COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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FINANCIAL ANALYSIS

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PUBLIC SERVICE COMMISSION

In the Matter of:

MODIFICATION TO WESTERN KENTUCKY GAS COMPANY, A DIVISION OF ATMOS ENERGY CORPORATION, GAS COST ADJUSTMENT TO INCORPORATE AN EXPERIMENTAL PERFORMANCE BASED RATEMAKING MECHANISM (PBR)	)	Case No. 2001-317

JOINT MOTION

Come now Western Kentucky Gas Company ("Western"), a division of Atmos Energy Corporation and the Attorney General of the Commonwealth of Kentucky, by and through his Office for Rate Intervention (the "Attorney General") and jointly move the Kentucky Public Service Commission for approval of the attached Settlement Agreement which has been duly executed by Western and the Attorney General.

Respectfully submitted this 18th day of February, 2002.

Mark R. Hutchinson
1700 Frederica Street
Suite 201
Owensboro, Kentucky 42301
Attorney for Western

Elizabeth E. Blackford
Assistant Attorney General
Capital Center Drive
Suite 200
Frankfort, Kentucky 40601

CERTIFICATE OF SERVICE

This is to certify that on the 18th day of February, 2002, the original of this Motion, together with ten (10) copies, were filed with the Kentucky Public Service Commission, 211 Sower Blvd., P.O. Box 615, Frankfort, Kentucky 40602.

Elizabeth E. Blackford

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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FEB 18 2002
PUBLIC SERVICE COMMISSION

In the Matter of:

MODIFICATION TO WESTERN KENTUCKY GAS COMPANY, A DIVISION OF ATMOS ENERGY CORPORATION, GAS COST ADJUSTMENT TO INCORPORATE AN EXPERIMENTAL PERFORMANCE BASED RATEMAKING MECHANISM (PBR)	)	Case No. 2001-317

SETTLEMENT AGREEMENT

THIS SETTLEMENT AGREEMENT is made and entered into this 18th day of February, 2002 by and between the Attorney General of the Commonwealth of Kentucky, by and through his Office for Rate Intervention (the "Attorney General") and Western Kentucky Gas Company ("Western").

WITNESSETH: That whereas, on September 28, 2001, Western, pursuant to the Commission's Order of June 1, 1998 in Case No. 97-513, submitted its report on the results of the three (3) year experimental Performance Based Ratemaking ("PBR") and further applied to the Commission for an Order modifying and extending Western's PBR for an additional term of five (5) years commencing as of April 1, 2002; and,

WHEREAS, the Commission assigned Western's aforesaid application Case No. 2001-317; and,

WHEREAS, on October 16, 2001, the Attorney General filed for full intervention in this proceeding to represent the consumers' interests; and,

WHEREAS, the Commission granted the Attorney General full intervention in this proceeding by Order dated October 19, 2001; and,

WHEREAS, pursuant to the Commission's procedural schedule extensive discovery has been exchanged by and among the parties and the Commission Staff; and,

WHEREAS, an informal conference among the Attorney General, Western and the Commission Staff was held pursuant to 807 KAR 5:001 Section 4 (4) in order to provide for the opportunity for settlement on January 29, 2002; and,

WHEREAS, as a result of that conference Western and the Attorney General have reached agreement on all issues relating to Western's pending application for modification and extension of its PBR; and,

WHEREAS, the Attorney General and Western have agreed to submit this settlement agreement to the Commission with the request that it be approved and adopted; and,

WHEREAS, the parties believe that the terms of the settlement set forth below are fair, just and reasonable and are in the best interest of Western and its ratepayers; and,

NOW THEREFORE, the parties hereby stipulate and agree to the following:

1. The Report filed by Western on September 28, 2001, concerning the results of its three (3) year experimental PBR should be accepted by the Commission.

2. Western's existing PBR, as modified in this settlement, should be extended for a term of four (4) years commencing as of the effective date contained in the Commission's final order in this proceeding. Western agrees to file its report concerning the results of the initial three (3) years of the PBR within sixty (60) days of the end of the third year.

3. Western's existing gas supply agreement will expire at the termination of Western's existing PBR. Upon entry of an order by the Commission approving this settlement agreement, Western agrees to promptly issue a request for proposal ("RFP") for a new gas supply contract to interested and qualified bidders. The RFP will include those terms set forth in Exhibit "A", page 3 of Western's Initial PBR Report, except as modified by this Settlement Agreement.

4. Under Western's current PBR, the sharing ratio under which variances between actual costs and benchmark costs are shared between ratepayers and shareholders is 50/50. The parties have agreed to modify the sharing ratio to provide for a sliding scale mechanism, having two bands. The first band will cover gas cost savings or excess gas costs from 0% up to and including 2.0%. The second band will cover variances of more than 2.0%. In the event Western enters into a third party gas supply agreement under paragraph 3 of this agreement, and for so long as gas is supplied

pursuant to that agreement, the sharing ratio for band one shall be 70/30 in favor of ratepayers. The sharing ratio for band two shall be 50/50. In the event Western does not award the gas supply contract or must otherwise commence "in-house" management and operation of its gas supply needs, then for so long as it engages in "in-house management" the sharing ratio for band one shall be 75/25 in favor of ratepayers and the sharing ratio for band two shall be 50/50.

5. As to the Gas Acquisition Index Factor ("GAIF"), for the purposes of issuing the RFP under paragraph three of this agreement, and in the event a third party gas supply agreement is issued under that paragraph, it is agreed that the simple average of the four current indices (<u>National Gas Week; Gas Daily; Inside F.E.R.C.'s Gas Market Report;</u> and, New York Mercantile Exchange (NYMEX)) for the Base Load will remain as currently specified in Western's tariffs. In the event Western does not award the gas supply contract of a third party or must otherwise commence "in-house" management and operation of its gas supply needs, the NYMEX closing prices will be removed from the GAIF as a benchmark index for Base Load and Western shall submit a revised tariff to that effect. However, as for intra-month swing purchases, <u>Gas Daily</u> will be the sole benchmark index.

6. As to the Transportation Index Factor ("TIF"), FERC approved pipeline transportation rates will continue to serve as the benchmarks against which Western's negotiated, discounted pipeline rates are measured. Additionally, the capacity release threshold ("CRT") required by the Commission in Western's initial PBR will be eliminated.

7. The existing Off-System Sales Index Factor ("OSSIF") will be modified to add off system sales of storage services. Western acknowledges that the Commission will closely monitor any such activity to insure that there is no detrimental impact on Western's system customers, either from a reliability perspective or from a cost perspective.

8. Western withdraws its request for a proposed Storage Development and Cost Recovery Factor ("SDRF") mechanism.

9. It is agreed that upon approval of this settlement agreement by the Commission, Western will file the attached amended tariff sheets which are marked as Exhibits "1", pages 29 A through 29 K.1, and which are incorporated herein by reference.

10. If the Commission accepts this settlement agreement, it will be necessary either to extend the contract between Woodward and Western or to have Western resume its gas supply operations itself between the date the Order is entered and a new contract is let under the RFP issued pursuant to paragraph 3 hereof, or a decision

is made that no new contract shall be let and Western will resume its own gas supply operations. Woodward has agreed to extend the contract with Western on a month to month basis during the interim period upon the same terms and conditions as the original contract. For purposes of this Settlement Agreement, "Interim Period" shall mean that period of time commencing as of the effective date of the Commission's order accepting this Settlement Agreement, and ending at such time as the Commission grants final approval to a new third party gas supply agreement entered into by Western pursuant to the provisions of paragraph 3 of this agreement or at such time as Western elects not to award a third party gas supply contract and commences "in-house" management and operation of its gas supply needs, whichever first occurs. Western shall report to the Commission that it has elected to commence "in-house" management of its gas supply needs or file an application for approval of a new third party gas supply agreement when the decision is made or the contract is placed, and in any event no later than three (3) months following the first day of the month following the month in which the order is entered. Under these circumstances the parties are agreed that the Woodward contract should be continued for the interim period. The benefits of the current PBR have been derived from the operation of the contract and the terms of that contract have been approved by the

Commission. An extension of the contract during the interim period is reasonable.

11. In the event the Commission accepts this Settlement Agreement, and in the further event Western's existing gas supply agreement is extended (the "Extended Agreement"), then and in those events, it is agreed that the amended tariff sheets attached hereto as Exhibit "1", pages 29 A through 29 K.1, will apply to all transactions under the Extended Agreement for the Interim Period.

In the event the Commission accepts this Settlement Agreement, the parties further request that the Commission's Order become effective on the first day of the month following the month in which the Commission enters such order.

12. This agreement is subject to the approval of the Commission. If the Commission fails to accept and approve this settlement agreement in its entirety, this proceeding will continue and neither the terms of this agreement nor any other matter raised during the settlement discussions will be admissible in any subsequent regulatory or judicial proceeding and will not be binding on either of the parties hereto.

13. If the Commission accepts and adopts this agreement in its entirety, neither the Attorney General nor Western will request any rehearing or bring any type of action for judicial review.

WITNESS the signatures of the parties hereto on this the day and date first hereinabove written.

ATTORNEY GENERAL OF THE COMMONWEALTH OF KENTUCKY

By: ______________________

WESTERN KENTUCKY GAS COMPANY

By: ______________________

Western Kentucky Gas Company
Modification of Performance-Based Ratemaking Mechanism

Case No. 2001-317

Exhibit 1

Proposed Tariff Pages 29A – 20K.1

Issue Date: February 18, 2002

WESTERN KENTUCKY GAS COMPANY

PBR

Experimental Performance Based Rate Mechanism (T)

Applicable

To all gas sold.

Rate Mechanism

The amount computed under each of the rate schedules to which this Performance Based Rate Mechanism is applicable shall be increased or decreased by the Performance Based Rate Recovery Factor (PBRRF) at a rate per 1,000 cubic feet (Mcf) of monthly gas consumption. Demand costs and commodity costs shall be accumulated separately and included in the pipeline suppliers Demand Component and the Gas Supply Cost Component of the Gas Cost Adjustment (GCA), respectively. The PBRRF shall be determined for each 12-month period ended October 31 during the effective term of these experimental performance based ratemaking mechanisms, which 12-month period shall be defined as the PBR period.

The PBRRF shall be computed in accordance with the following formula:

$$PBRRF = (CSPBR + BA) / ES$$

Where:

ES = Expected Mcf sales, as reflected in the Company's GCA filing for the upcoming 12-month period beginning February 1.

CSPBR = Company Share of Performance Based Ratemaking Mechanism savings or expenses. The CSPBR shall be calculated as follows:

$$CSPBR = TPBRR \times ACSP$$

Where:

ACSP = Applicable Company Sharing Percentage

TPBRR = Total Performance Based Ratemaking Results. The TPBRR shall be savings or expenses created during the PBR period. TPBRR shall be calculated as follows:

$$TPBRR = (GAIF + TIF + OSSIF)$$

ISSUED: February 18, 2002 EFFECTIVE:

(Issued by Authority of an Order of the Public Service Commission in Case No. 2001-317 dated).

ISSUED BY: William J. Senter Vice President – Rates & Regulatory Affairs

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

GAIF

GAIF = Gas Acquisition Index Factor. The GAIF shall be computed as follows:

$$GAIF = GAIFBL + GAIFSL$$

Where:

GAIFBL represents the Gas Acquisition Index Factor for Base Load system supply natural gas purchases.

GAIFSL represents the Gas Acquisition Index Factor for Swing Load system supply natural gas purchases.

GAIFBL

The GAIFBL shall be calculated by comparing the Total Annual Benchmark Gas Commodity Costs for Base Load (TABGCCBL) system supply natural gas purchases for the PBR period to the Total Annual Actual Gas Commodity Costs for Base Load (TAAGCCBL) system supply natural gas purchases during the same period to determine if any shared expenses or shared savings exist.

TABGCCBL represents the Total Annual Benchmark Gas Commodity Costs for Base Load gas purchases and equals the annual sum of the monthly Benchmark Gas Commodity Costs of gas purchased for Base Load (BGCCBL) system supply

BGCCBL represents Benchmark Gas Commodity Costs for Base Load gas purchases and shall be calculated on a monthly basis and accumulated for the PBR period. BGCCBL shall be calculated as follows:

$$BGCCBL = Sum [(APVBLi - PEFDCQBL) \times SAIBLi] + (PEFDCQBL \times DAIBL)$$

Where:

APVBL is the Actual Purchased Volumes of natural gas for Base Load system supply for the month. The APVBL shall include purchases necessary to cover retention volumes required by the pipeline as fuel.

WESTERN KENTUCKY GAS COMPANY

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

"i" represents each supply area.

PEFDCQBL are the Base Load Purchases in Excess of Firm Daily Contract Quantities delivered to WKG's city gate. Firm Daily Contract Quantities are the maximum daily contract quantities which Company can deliver to its city gate under its various firm transportation agreements and arrangements.

SAIBL is the Supply Area Index factor for Base Load to be established for each supply area in which Company has firm transportation entitlements used to transport its natural gas purchases and for which price postings are available. The five supply areas are TGT-SL (Texas Gas Transmission-Zone SL), TGT-1 (Texas Gas Transmission-Zone 1), TGPL-0 (Tennessee Gas Pipeline-Zone 0), and TGPL-1 (Tennessee Gas Pipeline-Zone 1), and TGC-ELA (Trunkline Gas Company-ELA).

The monthly SAIBL for TGT-SL, TGT-1, TGPL-0, TGPL-1, and TGC-ELA shall be calculated using the following formula:

$$SAIBL = [I(1) + I(2) + I(3) + I(4)] / 4$$

Where:

"I" represents each index reflective of both supply area prices and price changes throughout the month in these various supply areas.

The indices for each supply zone are as follows:

<u>SAIBL (TGT-SL)</u>

I (1) is the average of weekly <u>Natural Gas Week</u> postings for Texas Gas Transmission Corporation Zone SL: South Louisiana as Spot Prices on Interstate Pipeline Systems.
I (2) is the average of the daily high and low <u>Gas Daily</u> postings for Louisiana-Onshore South Texas Gas Zone SL averaged for the month.
I (3) is the <u>Inside FERC – Gas Market Report</u> first-of-the-month posting for Texas Gas Zone SL.
I (4) is the <u>New York Mercantile Exchange</u> Settled Closing Price.

WESTERN KENTUCKY GAS COMPANY

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

SAIBL (TGT-1)

I (1) is the average of weekly Natural Gas Week postings for Texas Gas Transmission Corporation Zone 1: North Louisiana as Spot Prices on Interstate Pipeline Systems.
I (2) is the average of the daily high and low Gas Daily postings for East Texas – North Louisiana Area - Texas Gas Zone 1 averaged for the month.
I (3) is the Inside FERC – Gas Market Report first-of-the-month posting for Texas Gas Zone 1.
I (4) is the New York Mercantile Exchange Settled Closing Price.

SAIBL (TGPL-0)

I (1) is the average of weekly Natural Gas Week postings for Tennessee Gas Pipeline Co. Zone 0: South Texas as Spot Prices on Interstate Pipeline Systems.
I (2) is the average of the daily high and low Gas Daily postings for Texas South – Corpus Christi – Tennessee and East Texas – North Louisiana Area – Tennessee, 100 leg averaged for the month.
I (3) is the Inside FERC – Gas Market Report first-of-the-month posting for Tennessee Zone 0.
I (4) is the New York Mercantile Exchange Settled Closing Price.

SAIBL (TGPL-1)

I (1) is the average of weekly Natural Gas Week postings for Tennessee Gas Pipeline Co. Zone 1: South Louisiana as Spot Prices on Interstate Pipeline Systems.
I (2) is the average of the daily high and low Gas Daily postings for Louisiana-Onshore South – 500 leg and – 800 leg average for the month.
I (3) is the Inside FERC – Gas Market Report first-of-the-month posting for Tennessee Zone 1.
I (4) is the New York Mercantile Exchange Settled Closing Price.

SAIBL (TGC-ELA)

I (1) is the average of weekly Natural Gas Week postings for Trunkline Gas Co. East Louisiana as Spot Prices on Interstate Pipeline Systems.
I (2) is the average of the daily high and low Gas Daily postings for Louisiana-Onshore South, Trunkline ELA.
I (3) is the Inside FERC – Gas Market Report first-of-the-month posting for Trunkline Louisiana.
I (4) is the New York Mercantile Exchange Settled Closing Price.

WESTERN KENTUCKY GAS COMPANY

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

DAIBL is the Delivery Area Index factor for Base Load to be established for purchases made by Company when Company has fully utilized its pipeline quantity entitlements on a daily basis and which are for delivery to Company's city gate from Texas Gas Transmission's Zone 2, 3 or 4, Tennessee Gas Pipeline's Zone 2, or Trunkline Gas Company's Zone 1B.

The monthly DAIBL for TGT-2, 3, 4, TGPL-2, and TGC-1B shall be calculated using the following:

$$DAIBL = [I(1) + I(2) + I(3)] / 3$$

DAIBL (TGT-2, 3, & 4), (TGPL-2) and (TGC-1B)

I (1) is the average of weekly Natural Gas Week postings for Spot Prices on Interstate Pipeline Systems for Dominion – South.
I (2) is the average of the daily high and low Gas Daily postings the Daily Price Survey for Dominion – South Point.
I (3) is the Inside FERC – Gas Market Report first-of-the-month posting for Prices of Spot Gas Delivered to Pipeline for Dominion Transmission Inc. – Appalachia.

TAAGCCBL represents Company's Total Annual Actual Gas Commodity Costs for Base Load deliveries of natural gas purchased for system supply and is equal to the total monthly actual gas commodity costs.

To the extent that TAAGCCBL exceeds TABGCCBL for the PBR period, then the GAIFBL Shared Expenses shall be computed as follows:

$$\text{GAIFBL Shared Expenses} = TAAGCCBL - TABGCCBL$$

To the extent that TAAGCCBL is less than TABGCCBL for the PBR period, then the GAIFBL Shared Savings shall be computed as follows:

$$\text{GAIFBL Shared Savings} = TABGCCBL - TAAGCCBL$$

WESTERN KENTUCKY GAS COMPANY

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

GAIFSL

The GAIFSL shall be calculated by comparing the Total Annual Benchmark Gas Commodity Costs for Swing Load (TABGCCSL) system supply natural gas purchases for swing load for the PBR period to the Total Annual Actual Gas Commodity Costs for Swing Load (TAAGCCSL) system supply natural gas purchases for during the same period to determine if any shared expenses or shared savings exist.

TABGCCSL represents the Total Annual Benchmark Gas Commodity Costs for Swing Load gas purchases and equals the monthly Benchmark Gas Commodity Costs of gas purchased for Swing Load system supply (BGCCSL).

BGCCSL represents Benchmark Gas Commodity Costs for Swing Load gas purchases and shall be calculated on a monthly basis and accumulated for the PBR period. BGCCSL shall be calculated as follows:

$$BGCCSL = \text{Sum}\ [(APVSLi - PEFDCQSL) \times SAISLi] + (PEFDCQSL \times DAISL)$$

Where:

APVSL is the Actual Purchased Volumes of natural gas for Swing Load system supply for the month. The APVSL shall include purchases necessary to cover retention volumes required by the pipeline as fuel.

"i" represents each supply area.

PEFDCQSL are the Purchases in Excess of Firm Daily Contract Quantities delivered to WKG's city gate. Firm Daily Contract Quantities are the maximum daily contract quantities which Company can deliver to its city gate under its various firm transportation agreements and arrangements.

SAISL is the Supply Area Index factor for Swing Load to be established for each supply area in which Company has firm transportation entitlements used to transport its natural gas purchases and for which price postings are available. The five supply areas are TGT-SL (Texas Gas Transmission-Zone SL), TGT-1 (Texas Gas Transmission-Zone 1), TGPL-0 (Tennessee Gas Pipeline-Zone 0), and TGPL-1 (Tennessee Gas Pipeline-Zone 1), and TGC-ELA (Trunkline Gas Company-ELA).

WESTERN KENTUCKY GAS COMPANY

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

The monthly SAISL for TGT-SL, TGT-1, TGPL-0, TGPL-1, and TGC-ELA shall be calculated using the following formula:

$$SAISLi = I(i)$$

Where:

"I" represents each index reflective of both supply area prices and price changes throughout the month in these various supply areas.

"i" represents each supply area.

The index for each supply zone is as follows:

SAISL (TGT-SL)

I (1) is the average of the daily high and low Gas Daily postings for Louisiana-Onshore South Texas Gas Zone SL averaged for the month.

SAISL (TGT-1)

I (2) is the average of the daily high and low Gas Daily postings for East Texas – North Louisiana Area - Texas Gas Zone 1 averaged for the month.

SAISL (TGPL-0)

I (3) is the average of the daily high and low Gas Daily postings for Texas South – Corpus Christi – Tennessee and East Texas – North Louisiana Area – Tennessee, 100 leg averaged for the month.

SAISL (TGPL-1)

I (4) is the average of the daily high and low Gas Daily postings for Louisiana-Onshore South – 500 leg and – 800 leg average for the month.

WESTERN KENTUCKY GAS COMPANY

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

SAISL (TGC-ELA)

I (5) is the average of the daily high and low Gas Daily postings for Louisiana-Onshore South, Trunkline ELA.

DAISL is the Delivery Area Index factor for Swing Load to be established for purchases made by Company when Company has fully utilized its pipeline quantity entitlements on a daily basis and which are for delivery to Company's city gate from Texas Gas Transmission's Zone 2, 3 or 4, Tennessee Gas Pipeline's Zone 2, or Trunkline Gas Company's Zone 1B.

The monthly DAISL for TGT-2, 3, 4, TGPL-2, and TGC-1B shall be calculated using the following:

DAISL = I(1)

DAISL (TGT-2, 3, & 4), (TGPL-2) and (TGC-1B)

I (1) is the average of the daily high and low Gas Daily postings the Daily Price Survey for Dominion – South Point.

TAAGCCSL represents Company's Total Annual Actual Gas Commodity Costs for Swing Load deliveries to Company's city gate and is equal to the total monthly actual gas commodity costs.

To the extent that TAAGCCSL exceeds TABGCCSL for the PBR period, then the GAIFSL Shared Expenses shall be computed as follows:

GAIFSL Shared Expenses = TAAGCCSL - TABGCCSL

To the extent that TAAGCCSL is less than TABGCCSL for the PBR period, then the GAIFSL Shared Savings shall be computed as follows:

GAIFSL Shared Savings = TABGCCSL - TAAGCCSL

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

TIF

TIF = Transportation Index Factor. The Transportation Index Factor shall be calculated by comparing the Total Annual Benchmark Transportation Costs (TABTC) of natural gas transportation services during the PBR period to the Total Annual Actual Transportation Costs (TAATC) applicable to the same period to determine if any shared expenses or shared savings exist.

The Total Annual Benchmark Transportation Costs (TABTC) are calculated as follows:

TABTC = Annual Sum of Monthly BTC

Where:

BTC is the Benchmark Transportation Costs which include both pipeline demand and volumetric costs associated with natural gas pipeline transportation services. The BTC shall be accumulated for the PBR period and shall be calculated as follows:

BTC = Sum [BM (TGT) + BM (TGPL) + BM (TGC) + BM (PPL)]

Where:

BM (TGT) is the benchmark associated with Texas Gas Transmission Corporation.

BM (TGPL) is the benchmark associated with Tennessee Gas Pipeline Company.

BM (TGC) is the benchmark associated with Trunkline Gas Company.

BM (PPL) is the benchmark associated with a proxy pipeline. This benchmark, which will be determined at the time of purchase, will be used to benchmark purchases of transportation capacity from non-traditional sources.

The benchmark associated with each pipeline shall be calculated a follows:

BM (TGT) = (TPDR x DQ) + (TPCR x AV) + S&DB
BM (TGPL) = (TPDR x DQ) + (TPCR x AV) + S&DB
BM (TGC) = (TPDR x DQ) + (TPCR x AV) + S&DB
BM (PPL) = (TPDR x DQ) + (TPCR x AV) + S&DB

Where:

TPDR is the applicable Tariffed Pipeline Demand Rate.

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

DQ is the Demand Quantities contracted for by the Company from the applicable transportation provider.

TPCR is the applicable Tariffed Pipeline Commodity Rate.

AV is the Actual Volumes delivered at Company's city gate by the applicable transportation provider for the month.

S&DB represents Surcharges, Direct Bills and other applicable amounts approved by the Federal Energy Regulatory Commission (FERC). Such amounts are limited to FERC approved charges such as surcharges, direct bills, cashouts, take-or-pay amounts, Gas Supply Realignment and other Order 636 transition costs.

The Total Annual Actual Transportation Costs (TAATC) paid by Company for the PBR period shall include both pipeline demand and volumetric costs associated with natural gas pipeline transportation services as well as all applicable FERC approved surcharges, direct bills included in S&DB, less actual capacity release credits. Such costs shall exclude labor related or other expenses typically classified as operating and maintenance expenses.

To the extent that TAATC exceeds TABTC for the PBR period, then the TIF Shared Expenses shall be computed as follows:

TIF Shared Expenses = TAATC - TABTC

To the extent that the TAATC is less than TABTC for the PBR period, then the TIF Shared Savings shall be computed as follows:

TIF Shared Savings = TABTC - TAATC

Should one of the Company's pipeline transporters file a rate change effective during any PBR period and bill such proposed rates subject to refund, the period over which the benchmark comparison is made for the relevant transportation costs will be extended for one or more 12 month periods, until the FERC has approved final settled rates, which will be used as the appropriate benchmark. Company will not share in any of the savings or expenses related to the affected pipeline until final settled rates are approved.

OSSIF

OSSIF = Off-System Sales Index Factor. The Off-System Sales Index Factor shall be equal to the Net Revenue from Off System Sales (NR).

WESTERN KENTUCKY GAS COMPANY

PBR

Experimental Performance Based Rate Mechanism (Continued) (T)

Net Revenue is calculated as follows:

$$NR = OSREV - OOPC$$

Where:

OSREV is the total revenue associated with off-system sales and storage service transactions.

OOPC is the out-of-pocket costs associated with off-system sales and storage service transactions and shall be determined as follows:

$$OOPC = OOPC(GC) + OOPC(TC) + OOPC(SC) + OOPC(UGSC) + \text{Other Costs}$$

Where:

OOPC (GC) is the Out-of-Pocket Gas Costs associated with off-system sales transactions. For off-system sales utilizing Company's firm supply contracts, the OOPC (GC) shall be the incremental costs to purchase the gas available under Company's firm supply contracts. For off-system sales not using Company's firm supply contracts, the OOPC (GC) shall be the incremental costs to purchase the gas from other entities.

OOPC (TC) is the Out-of-Pocket Transportation Costs associated with off-system sales transactions. For off-system sales utilizing Company's firm transportation agreements, the OOPC (TC) shall be the incremental cost to use the transportation available under Company's firm supply contracts. For off-system sales not using Company's firm transportation agreements, the OQPC (TC) shall be the incremental costs to purchase the transportation form other entities.

OOPC (SC) is the Out-of-Pocket Storage Costs associated with off-system sales of storage. If this is gas in Company's own storage or gas stored with Tennessee Gas Pipeline it shall be priced at the average price of the gas in Company's storage during the month of sale. If this is gas from the storage component of Texas Gas's No-Notice Service, this gas shall be priced at the replacement costs.

OOPC (UGSC) is the Out-of-Pocket Underground Storage Costs associated with off-system sales of storage services. For the off-systems sales of storage services utilizing Company's on-system storage, the OOPC(UGSC) shall include incremental storage losses, odorization, and other fuel-related costs such as purification, dehydration, and compression. Such costs shall exclude labor-related expenses.

Other Costs represent all other incremental costs and include, but are not limited to, costs such as applicable sales taxes and excise fees. Such costs shall exclude labor-related or other expenses typically classified as operating and maintenance expenses.

WESTERN KENTUCKY GAS COMPANY

PBR

Experimental Performance Based Rate Mechanism (Continued)

ACSP

ACSP = Applicable Company Sharing Percentage. The ACSP shall be determined based on the PTAGSC.

Where:

PTAGSC = Percentage of Total Actual Gas Supply Costs. The PTAGSC shall be the TPBRR stated as a Percentage of Total Actual Gas Supply Costs and shall be calculated as follows:

PTAGSC = TPBRR / TAGSC

Where:

TAGSC = Total Actual Gas Supply Costs. The TAGSC shall be calculated as follows:

TAGSC = TAAGCCBL + TAAGCCSL + TAATC

If the absolute value of the PTAGSC is less than or equal to 2.0%, then the ACSP of 30% shall be applied to TPBRR to determine CSPBR. If the absolute value of the PTAGSC is greater than 2.0%, then the ACSP of 30% shall be applied to the amount of TPBRR that is equal to 2.0% of TAGSC to determine a portion of CSPBR, and the ACSP of 50% shall be applied to the amount of TPBRR that is in excess of 2.0% of TAGSC to determine a portion of CSPBR. These two portions are added together to produce the total CSPBR.

BA

BA = Balance Adjustment. The BA is used to reconcile the difference between the amount of revenues billed or credited through the CSPBR and previous application of the BA and revenues which should have been billed or credited, as follows:

1. For the CSPBR, the balance adjustment amount will be the difference between the amount billed in a 12 month period from the application of the CSPBR and the actual amount used to establish the CSPBR for the period.

2. For the BA, the balance adjustment amount will be the difference between the amount billed in a 12-month period from the application of the BA and the actual amount used to establish the BA for the period.

Review

Within 60 days of the end of the third year of the four-extension, the Company will file an assessment and review of the PBR mechanism for the first three years of the extension period. In that report and assessment, the Company will make any recommended modifications to the PBR mechanism.

ISSUED: February 18, 2002 **EFFECTIVE:**

(Issued by Authority of an Order of the Public Service Commission in Case No. 2001-317 dated)

ISSUED BY: William J. Senter Vice President – Rates & Regulatory Affairs