ATMOS ENERGY CORPORATION
KENTUCKY PUBLIC SERVICE COMMISSION
CASE NO. 2005-00321
DATED: OCTOBER 4, 2005
DUE: OCTOBER 21, 2005

SUPPLEMENTAL DATA REQUEST – OFFICE OF THE ATTORNEY GENERAL
DATA REQUEST NO. 1

QUESTION: What role does asset management play in gas supply apart from a performance based rate?

RESPONSE:

The asset management model has been utilized by Atmos Energy since inception of the Performance Based Rate mechanism in 1998. Under this model, the Company arranges to receive full requirements supply from a single entity who also manages the Company's assets from day to day.

The asset manager is afforded the opportunity to optimize the assets not needed by the utility from time to time and generate revenues from on-system and off-system utilization of the idle assets. As a result, the Company and its customers are able to glean savings by affording asset management rights to the full requirements supplier.

SUBMITTED BY: Gary Smith

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SUPPLEMENTAL DATA REQUEST – OFFICE OF THE ATTORNEY GENERAL
DATA REQUEST NO. 2

QUESTION: How important is asset management to gas supply?

RESPONSE:

Refer also to the Company's response to DR # 1 of this AG supplemental data request.

Assignment of the management of all of Atmos Energy's Kentucky firm transportation and storage contracts to the "full-requirements" supplier has proven to be a beneficial contract feature. The objective of Atmos Energy's supply contract is to ensure reliability and extract the lowest cost bid possible from potential bidders through the enticement offered by the largest and most comprehensive contract possible. The Request For Proposal combines the Company's full firm gas commodity requirements with all of its upstream transportation and storage contracts. Hence, potential suppliers are assured of the opportunity to supply Atmos Energy's large, firm market for multiple years plus the additional opportunity to leverage the substantial transportation capacity and storage assets beyond the actual supply requirements of that firm market from time to time when operationally feasible. Despite the breadth and supplier flexibility inherent in a full-requirements contract, the Company also retains full operational control through mandatory compliance with a prescribed seasonal storage and operational plan, and non-performance penalties and remedies.

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SUPPLEMENTAL DATA REQUEST – OFFICE OF THE ATTORNEY GENERAL
DATA REQUEST NO. 3

QUESTION: Would Atmos agree that having an asset management fee that is not tied to volume decouples wholesale price paid from retail price?

RESPONSE:

No.

The Company created the asset management fee allowance to permit creative bid structure options for prospective bidders, allowing for a fixed discount component not expressed in per volume terms. The fixed discount component, or asset management fee, would still be tied to the obligation for full requirements supply volumes. The tariff formula, currently, is based upon an expectation of solely a "cents off" discount to the gas commodity market basket of indices. The Company has no preference as to whether a bidder submits an index-based bid or a bid that incorporates a fixed discount component. The new addition to the tariff formula merely provides an option for bidders, from which the Company will choose the best bid.

The value of the Company's assets to any prospective bidder are not likely directly tied to the volume changes which will occur from year to year, primarily due to weather variations. During years of colder than normal weather, the Company's volume requirements would increase and its utilization of assets such as interstate capacity and storage would be increased as well. Under these conditions, the idle assets available to the Supplier would be less available. This example shows the mismatch between a Supplier volumetric discount which becomes greater with higher volumes, while arguably lowering the availability of the assets they can leaverage.

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SUPPLEMENTAL DATA REQUEST – OFFICE OF THE ATTORNEY GENERAL
DATA REQUEST NO. 4

QUESTION: Please state why it is appropriate to disassociate the concept of volume at the wholesale level, when Atmos and all other LDC's charge by volume at the retail level.

a. What assurance is there that the actual cost Atmos pays for gas at the wholesale level, on a basis different than volume, would somehow be accurately translated to a volumetric basis on the retail level?
b. How does Atmos propose to attribute the amount of any discount achieved through gas supply management, which may not be measured on a volumetric basis, to the retail customer, who always pays on a volumetric basis?
c. If the asset management fee does not vary with volume, how will savings credit offset against volume? Will the offset be higher per mcf in low volume years and lower per mcf in high volume years?

RESPONSE:

The Company, in this proposal, does not believe it is disassociating the concept of volume at the wholesale level. We merely believe there could be enhanced value to prospective supply bidders by allowing a fixed component in their bid structure.

a. The cost of gas would flow through the PGA in the same manner that it flows today. The Company could require the asset management fee to be paid, or credited toward supply costs on a uniform monthly basis. The fixed discount would then be reflected in the process of projecting gas costs and applying the discount in the reconciliation of actual costs, at the time they are available. The tariff proposed in this Case would establish the process for considering such a discount in the computation of PBR recoveries.

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RESPONSE:

b. If the Company was to award the supply agreement to a bidder that incorporated an asset management fee into their bid, the Company would reflect those savings in a manner similar to other gas costs that are not volumetric in nature, such as interstate demand charges. Please also refer to DR # 4(a) of this AG data request.

c. The benefit of an asset management fee is that the guaranteed payment (or discount) is not affected by weather-related volume changes of the market. This structure would ensure a constant level of savings. Yes, on a per unit basis, the savings would be higher in low volume years and lower in high volume years, but the burden would purely be on the agent to provide the fixed discount component regardless of the volumes delivered.

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SUPPLEMENTAL DATA REQUEST – OFFICE OF THE ATTORNEY GENERAL
DATA REQUEST NO. 5

QUESTION: Please state why Atmos' PBR should be made permanent when Atmos has just developed and plans to employ an entirely new benchmark concept, that of the GAIFAM. Would Atmos agree that it is more appropriate that Atmos' PBR continue on a pilot basis when it establishes the new measures of performance?

RESPONSE:

The Company has proposed a five (5) year extension of the PBR in its Application. In an earlier response to DR # 4 of the First Data Request of Commission Staff, the Company acknowledged it would be open to a permanent implementation of the PBR tariff.

The referenced GAIFAM was introduced purely to give prospective vendors more flexibility in their bids in response to our Request For Proposals. There is no certainty that the vendor awarded the supply contract will incorporate an asset management fee structure in their bid.

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SUPPLEMENTAL DATA REQUEST – OFFICE OF THE ATTORNEY GENERAL
DATA REQUEST NO. 6

QUESTION: Please state whether the GAIFAM is connected in any way to any industry practice or standard.

RESPONSE:

The Company is seeing more asset management fees incorporated into responses to Requests For Proposals. The Company is attempting to create flexibility in the proposals submitted by prospective suppliers by accommodating the GAIFAM; the Company is not requiring or favoring an asset management fee structure, however.

Please also refer to the Company's response to DR # 2 of the Supplement Data Request from Commission Staff.

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SUPPLEMENTAL DATA REQUEST – OFFICE OF THE ATTORNEY GENERAL
DATA REQUEST NO. 7

QUESTION: KRS 278.272 provides as follows:

Consideration of natural gas purchasing transaction in determining just and reasonable rates; limitation of authorized rate of return for natural gas operations.

"In determining just and reasonable rates, the commission shall investigate and review natural gas purchasing transactions of a utility, whose rates for retail sales of natural gas are regulated by the commission, from an affiliate. The commission shall limit the authorized rate of return of the utility for its natural gas operations to a level which, when considered with the level of profit or return the affiliate earns on natural gas transactions to such utility, is just and reasonable." [Emphasis added]

Please state what measures the Commission has taken to investigate and review Atmos' purchase of gas from its affiliate.

RESPONSE:

The Commission conducted a thorough review of gas procurement practices of Atmos Energy and the other four large gas utilities in Kentucky, utilizing an independent consultant, Liberty Consulting, in that effort. The report, published in November 2002, addressed specific findings and recommendations regarding Atmos Energy's gas supply planning, organization & controls, supply management, transportation programs, balancing, response to regulatory change and affiliate relations. Additionally, report chapters common to the five Kentucky LDC's addressed natural gas price issues, impacts of hedging, GCA mechanisms, forecasting and impacts of affiliate relationships.

Atmos Energy received a favorable review in that comprehensive audit. Atmos Energy received nine recommendations for process improvements, among which were improvements to our RFP process, which will be employed in the upcoming asset management RFP. In regard to their review of affiliate relations, Liberty concluded Atmos

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RESPONSE:

Energy's transactions were appropriate and had no recommendations for improvements.

Atmos Energy has continued to work closely with the management audit staff implementing the recommended gas procurement audit improvements.

In addition, the Company must file and the Commission must approve each change in the Company's gas costs before they are passed on to customers. With regard to Atmos Energy's gas costs, the Company is typically the lowest or second lowest cost provider in the State.

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SUPPLEMENTAL DATA REQUEST – OFFICE OF THE ATTORNEY GENERAL
DATA REQUEST NO. 8

QUESTION: KRS 278.274 provides, in pertinent part, as follows:

Review of natural gas utility's purchasing practices in determining reasonableness of proposed rates; reduction of rates by commission

(1) In determining whether proposed natural gas utility rates are just and reasonable, the commission shall review the utility's gas purchasing practices. The commission may disallow any costs or rates which are deemed to result from imprudent purchasing practices on the part of the utility.
(2) When proposing new rates, the utility shall be required to prove that the proposal is just and reasonable in accordance with the requirements of this section.
(3) It shall be presumed that natural gas purchases from affiliated companies are not conducted at arm's length...

a. Please state how the Commission will be able to determine whether Atmos' purchase of gas will be fair, reasonable and prudent when the wholesaler grants a gas purchase price discount, and in exchange acquires the right to use Atmos' assets.
b. In the event Atmos' gas supplier is an affiliate, please state how the Commission will be able to determine Atmos' profit return based on its gas purchases from its affiliate.
c. Please state how the fact that a PBR is in place reveals that Atmos in engaging in prudent practices.

RESPONSE:

a. The PBR process is an established and proven model through which pudency review is streamlined due to the establishment of pre-determined gas cost benchmarks and the competitive bidding process employed in awarding the asset management contract. While a prudence review is not a part of this model, the Commission through its review and approval of the PBR, establishes a benchmark against which all purchases are measured. Thus, the

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RESPONSE:

benchmark, in effect, provides a surrogate for a prudence review. The benchmark makes it clear to everyone in advance what the specific standard for recovery of the costs will be. The current benchmark was established through a settlement to which the Attorney General's office was a signatory.

b. The Commission can, and will, determine Atmos Energy's "profit return" based on its gas purchases from an affiliate (the witness assumes "profit return" is intended to mean the same as "rate of return") in the same manner as it determines a fair and just rate of return in all general rate adjustment proceedings; by analyzing a vast amount of information concerning the utility and its operations and then applying well established rate making principals to arrive at a fair and just rate of return. The PBR mechanism at issue in the current proceeding has not, and will not, limit or in any way interfere with the Commission establishing just and reasonable rates for Atmos Energy and its customers.

c. Please refer to the Company's response to DR # 7 and DR # 8 (a) of this supplemental AG data request.

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