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January 14, 2022

Linda C. Bridwell
Executive Director
Public Service Commission
211 Sower Blvd.
Frankfort, KY 40601

Re: Atmos Energy Corporation
Case No. 2021-00214

Dear Ms. Bridwell:

Atmos Energy Corporation submits its brief. I certify that the electronic documents are true and correct copies of the original documents and that no party has been excused from electronic service.

If you have any questions about this filing, please contact me.

Submitted By:

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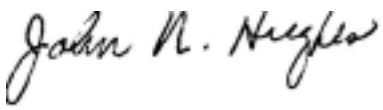

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Attorneys for Atmos Energy Corporation

BEFORE THE PUBLIC SERVICE COMMISSION

COMMONWEALTH OF KENTUCKY

APPLICATION OF ATMOS ENERGY	**)**	
	)	
CORPORATION FOR AN ADJUSTMENT	**)**	**Case No. 2021-00214**
	)	
OF RATES AND TARIFF MODIFICATIONS	**)**	

BRIEF OF ATMOS ENERGY CORPORATION

COMES NOW Atmos Energy Corporation ("Atmos Energy" or the "Company") and files this brief in the above-styled matter.

I. STATEMENT OF THE CASE

A. Introduction

Atmos Energy currently serves approximately 179,900 customers throughout its service area extending from western to central Kentucky. Residential class customers account for the majority of meters, at approximately 159,800. Atmos Energy's natural gas deliveries totaled approximately 47.7 Bcf during the 12-month period ending March 2021.

Atmos Energy originally sought Commission approval of an increase in annual revenue of $16,389,804.00. Through the discovery process and discussions with the parties, the Company has made adjustments to the filing resulting in a revised revenue requirement of $14,806,146 as incorporated in Exhibit JTC-R-1 of Company witness Joe Christian's rebuttal testimony. This results in an average monthly increase in residential bills of $4.54, representing an 8.8 % increase.

If approved, the new rates will increase revenues sufficiently to provide an overall rate of return on rate base of 7.63% on the adjusted test year rate base of $581,183,549. The actual increases by amount and percentage for each customer class are listed in the schedule attached as Exhibit 1 to this Brief. The rate calculation confirming the rates generate the revenue proposed is attached as Exhibit 2.

The relief requested in this proceeding is designed to maintain the general balance of fixed and variable elements in the distribution rates, reflect the underlying costs, characteristics of service, mitigate depletion of revenue caused by increased operating costs and capital investments in Kentucky.

B. Procedural History of the Case

On May 21, 2021, Atmos Energy filed with the Public Service Commission ("Commission") a notice of its intent to electronically file a general rate case ("Notice"). A copy of that notice was also served on the Kentucky Attorney General's Office of Rate Intervention ("OAG").

On June 30, 2021, Atmos Energy filed its application for an adjustment of rates and tariff modifications, effective July 30, 2021. By its letter dated July 2, 2021, the Commission notified Atmos Energy of certain filing deficiencies. On July 23, 2021, the Commission Staff notified Atmos Energy that its application met all minimum filing requirements.

On July 23, 2021, the Commission entered an Order, inter alia: (1) ordering that Atmos Energy's application be deemed filed as of that date; (2) suspending Atmos Energy's proposed rates for six (6) months, up to and including February 18, 2022; and (3) adopting a procedural schedule for this proceeding.

On July 8, 2021, the OAG filed its motion for full intervention, which was granted by the Commission's Order of July 16, 2021. The OAG is the only intervenor in this proceeding.

Atmos Energy responded to six discovery requests by the Commission staff and two sets of data requests by the OAG. A public hearing on Atmos Energy's application for an adjustment of rates and modification to tariffs was scheduled to begin on December 14, 2021. However, due to the tornados in portions of Atmos Energy's service area, the parties and Commission agreed to postpone the hearing. An additional round of discovery was scheduled to be followed by simultaneous briefs. Depending on the Commission's review of the responses and briefs, the need for a hearing will be re-

evaluated. Atmos Energy and the OAG waived having a hearing in a joint motion filed on December 13, 2021.

C. Summary of Atmos Energy's Proposed Adjustments and Other Relief

Atmos Energy originally sought Commission approval of an increase in annual revenue of $16.389 million. Subsequently, the Company filed a revised base rate increase of $15.052 million as reflected in Atmos Energy's Supplemental Response on August 23, 2021 to Staff's First Request, Item 55 to remove the impact of Winter Storm Uri on the Company's deferred tax asset ("DTA") net operating loss ("NOL") related to regulated operations. During rebuttal testimony, the Company also modified OAG recommendations on Rate Case Expense Amortization, SSU Division 002 T-Lock Adjustment-Unrealized Gains Liability ADIT, and Other SSU Division 002 ADIT deferred tax items as set forth in the rebuttal testimony of Atmos Energy witness Joe Christian.[1]

As a result of these adjustments, the total impact of the Staff First Request, Item 55 corrections as well as the modifications made within rebuttal testimony results in a request to increase annual revenue of $14,806,146 as incorporated in Exhibit JTC-R-1 of Company witness Joe Christian's rebuttal testimony. If approved, the new rates will increase revenues sufficiently to provide an overall rate of return on rate base of 7.63% on the adjusted test year rate base of $581,183,549.[2].

D. Key Issues

1. Rate Base Issues
2. Operating Income Issues
3. Cost of Capital
4. Return on Equity
5. Proposed Change to the Scope of Atmos Energy's Pipeline Replacement Program ("PRP")

[1] *See* Christian Rebuttal Testimony at 3-6.
[2] *See* Christian Rebuttal Testimony, Exhibit JTC-R-1

6. Appropriate Cost of Capital to Support Investment

7. Tax Act Adjustment Factor

8. Flexibility of Capital Investment Needed to Support Safety and Economic Growth

9. Lobbying Expense

10. Miscellaneous Fees

E. Legal Standard

KRS 278.190(1) establishes the procedure to be followed when a rate change is sought, referred to as a general rate case. KRS 278.192 states that for the purpose of justifying the reasonableness of a proposed general increase in rate, the commission **shall allow** a utility to utilize either an historical test period. . .or a forward-looking test period . . . .Thus, utilities have the **option** to file their rate cases using either: (1) a twelve (12) month historic test period that may include adjustments for known and measurable changes; or a fully forecasted test period presented in the form of pro forma adjustments to the base period. 807 KAR 5:001(16)(1)(a).

In this case, as it has in its previous seven rate cases in Kentucky, Atmos Energy elected to proceed with a fully forecasted test period because it believes this method presents a more accurate portrayal of the Company's revenue requirement. Under KRS 278.190(3), "at any hearing involving the rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the utility . . . ." The utility must show by substantial evidence the reasonableness of its test-period expenses and any proposed adjustments to those expenses, as well as the methodology used to determine its revenue requirement. An applicant in a "future test-period" case may carry its burden by providing the Commission with at least "some assurance that the expense will be incurred." "In the Matter of Alternative Rate Filing Adjustment for Delaplain Disposal Co.," Order, P.S.C. Case No. 2010-00349, p.12 (June 29, 2011).

Under Kentucky law, the Company is entitled to receive "fair, just and reasonable rates" for the services it provides. KRS 278.030(1). There is no single prescribed method for establishing rates. Kentucky Industrial Utility Customers, Inc. v. Kentucky Utilities Co., 983 S.W.2d 493 (Ky. 1998). KRS 278.030 and KRS 278.040 expressly grant the PSC plenary rate-making authority. KRS 278.030 provides that "[e]very utility may demand, collect and receive fair, just and reasonable rates for the services rendered or to be rendered by it to any person."

A utility's rates must, however, provide enough revenue to cover its operating expenses and the cost of capital. Federal Power Comm'n v. Hope Natural Gas Co., 320 U.S. 591 (1944). As our own Kentucky high court has stated, when establishing rates, the Commission must ensure the resulting rates will, inter alia, "…enable the utility to operate successfully, to maintain its financial integrity [and] to attract capital." Commonwealth ex rel Stephens v. South Central Bell Telephone Co., 545 S.W.2d 927, 930-31 (Ky. 1976).

Kentucky law allows a utility to "receive fair, just and reasonable rates for the services rendered or to be rendered by it to any person." KRS 278.030(1). As Kentucky courts have explained, "there is no litmus test for establishing fair, just and reasonable rates, and there is no single prescribed method for accomplishing that goal." Kentucky Indus. Util. Customers, Inc. v. Kentucky Utils. Co., 983 S.W.2d 493 (Ky. 1998). See also National-Southwire Aluminum Co. v. Big Rivers Electric Corp., 785 S.W.2d 503 (Ky. Ct. App. 1990).

Kentucky follows the rule set forth by the U.S. Supreme Court in Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1944). Hope made clear that, "[u]nder the statutory standard of 'just and reasonable' it is the result reached not the method employed which is controlling." Hope, 320 U.S. at 602. This results-oriented approach has been reaffirmed several times. See, e.g., Fed. Power Comm'n v. Memphis Light, Gas & Water Division, 411 U.S. 458, 474 (1973) ("under

Hope Natural Gas rates are 'just and reasonable' only if consumer interests are protected and if the financial health of the pipeline in our economic system remains strong."

The Hope decision gives the Commission "broad discretion in [the] factors to be considered in rate-making." National-Southwire, 785 S.W.2d at 512-13. The Commission may consider a utility's history and development, debt retirement and operating costs. National-Southwire, 785 S.W.2d at 512. Because of the constitutional requirement for non-confiscatory rates, the Hope Court identified "the financial integrity of the company whose rates are being regulated" as one of the major factors to be considered in ratemaking. Hope, 320 U.S. at 603. Ensuring financial viability would appear to be the very purpose of having fair, just, and reasonable rates. The United States Supreme Court has also suggested that rates "threatening [a utility's] 'financial integrity'" are "so unjust as to be confiscatory." Verizon Communs., Inc. v. Fed. Commun. Comm'n, 535 U.S. 467, 524 (2002) (quoting Duquesne Light Co., 488 U.S. at 307, 312. In other words, a utility's rates must provide "enough revenue not only for operating expenses but also for the capital costs of the business.") Hope, 320 U.S. at 603. Financial integrity of a utility is reflected in the longstanding principle that a "return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate under efficient and economical management to maintain its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield Waterworks v. Public Serv. Comm'n of W Va., 262 U.S. 679 (1923). Consequently, when setting rates that are fair, just, and reasonable, the Commission must ensure that the resulting rates will "enable the utility to operate successfully, to maintain its financial integrity, [and] to attract capital." Commonwealth ex rel Stephens v. South Central Bell Telephone Co., 545 S.W.2d 927, 930-31 (Ky. 1976). Approved rates must “enable the utility to operate successfully, to maintain its financial integrity, to attract capital and to compensate its investors for the risks assumed.” National Southwire, 785 S.W.2d 503, 512-513 (Ky. 1976).

F. Credibility and Weight of Evidence

Atmos Energy has provided detailed financial information which fully supports its request for rate relief in this proceeding. The written testimony, exhibits and data responses more than meet the substantial evidence standard. As such, the Company believes the evidence is sufficiently probative to compel findings consistent with the Company's request. Lee v. International Harvester Co. 373 S.W.2d 418 (Ky, 1963).

In contrast to the evidence provided by Atmos Energy, the OAG has failed to provide credible evidence on the issues it has raised in this case. As this Commission has held, when opinions are unsupported by any "factual evidence" they must be rejected. Administrative Case No. 273, Order ¶ 8, (Ky. PSC July 5, 1983). Kentucky courts have criticized reliance on testimony supported only on the witness's bare assertions. "Neither Daubert nor the rules of evidence require a trial court 'to admit opinion evidence that is connected to existing data only by the ispe dixit of the expert"'. Goodyear Tire & Rubber Co. v. Thompson, Ky. 11 S.W.3d 575, 581 (2000).

It is the Commission that must determine the credibility of the witnesses and the weight to be given to their testimony. Energy Regulatory Com. v. Kentucky Power Company, 605 S.W.2d 46, 50 (Ky. App. 1980). The weight of evidence is gauged by the credibility of the witnesses. "An Adjustment of Rates of Union Light and Power Company and Abandonment of Facilities," Order, Case Nos. 8419 and 8373 (Ky. PSC May 25, 1982). "The administrative trier of fact has the exclusive province to pass on the credibility of the witnesses and the weight of evidence." Energy Regulatory Com, 605 S.W.2d at 50. When closely analyzed and with very limited exceptions, the unsupported opinions of the OAG's witnesses as explained throughout this Brief, are insufficient to overcome the detailed factual and financial information provided by the Company.

II. ARGUMENT

In addition to the areas of no disagreement between the parties noted in the sections below, Atmos Energy notes that the OAG proposed no adjustments to the Company's revenue at present rates (supported by Company witness Densman), depreciation rates (supported by Company witness Watson), class cost of service (supported by Company witness Raab) or proposed tariff modifications with the exceptions of inclusion of Aldyl-A in the Company's Pipeline Replacement Program ("PRP") and Tax Act Adjustment Factor ("TAAF").

A. Rate Base Issues

1. Areas of No Disagreement Between the Parties

a. Tariff revisions:

1. Maintain the general balance of fixed and variable elements in our distribution rates to reflect the underlying cost characteristics of our service. This issue is discussed in detail by Paul Raab and Brannon Taylor in Direct testimony.
2. The revision of the Rate Book Index on Sheet Nos. 1 and 2 to reflect the changes described below. There is no revenue impact associated with this change.
3. The removal of the word "experimental" from the Company's PBR mechanism from Sheet Nos. 2 and 18.[3]
4. The removal of parking service and references to parking service from the Company's Tariff on Sheet Nos. 47, 48, 54, 55, and 60. This tariff modification would affect customers under Company's Rate Schedules T-3 and T-4.[4]
5. The replacement of the Natural Gas Weekly pricing index with the Gas Daily pricing index for imbalance pricing calculations on Sheets Nos. 48 and 55. This tariff modification would affect customers under Company's Rate Schedules T-3 and T-4.[5]
6. The following changes on Sheet No. 87 to the Priorities of Curtailment: (1) Combine all Commercial service under Rate G-1 into Priority Level 2; (2) Combine Industrial service under Rate G-1 and Rate T-4 Service to new Priority Level 3; (3) Combine service under Rate G-2 Service and Rate T-3 Service to new Priority Level 4; and (4) Make Flex Sales Transactions new Priority Level 5.[6]

[3] *See* Taylor Direct Testimony at 18-19.
[4] *See* Taylor Direct Testimony at 19-20; Atmos Energy's Response to Staff's Second Request, Items 8 and 9.
[5] *See* Taylor Direct Testimony at 20; Atmos Energy's Response to Staff's Second Request, Item 10
[6] *See* Taylor Direct Testimony at 21; Atmos Energy's Response to Staff's Second Request, Items 11 and 12.

> 7. Create the ability to issue Operational Flow Orders to transportation customers and their marketers on Sheet Nos. 88A and 88B. This tariff modification would affect customers under Company's Rate Schedules T-3 and T-4 and would require actions by Customers to alleviate conditions that, in the sole judgment of Company, jeopardize the operational integrity of Company's system.[7]

b. Exclusion of the Impact of Winter Storm Uri

After reviewing the OAG's discovery, the Company removed the impact of winter storm Uri on its deferred tax asset ("DTA") net operating loss ("NOL") related to regulated operations[8].

c. SSU Division 002 T-Lock Adjustment-Unrealized Gains Liability ADIT

As more fully explained by Company witness Joel Multer in his Rebuttal testimony, the Company agrees with Mr. Kollen that unrealized gains on interest rate contracts have been included in the common equity used to calculate weighted average cost of capital in this filing. As a result of the inclusion of unrealized gains in the Company's common equity, the Company concedes that an element of income tax expense associated with unrealized gains is included in the revenue deficiency determination. Because no cash tax payments are owed the taxing authorities in relation to unrealized gains on interest rate contracts, the Company does not object to Mr. Kollen's recommendation so long as there is no reduction to the common equity component used to calculated weighted average cost of capital in the Company's filing.[9] The Company has updated its base period and forecast period revenue requirement to include deferred tax items in rate base related to long-term financing, subject to the corresponding amounts being reflected in the Company's capital structure.

d. Other SSU Division 002 ADIT

As more fully explained by Company witness Joel Multer in his Rebuttal testimony, the

[7] *See* Taylor Direct Testimony at 22.
[8] Atmos Energy's Response to OAG's First Request, Item 20, subpart (c); Kollen Direct Testimony at 9. Please note that the Company had already removed the impact on its capital structure in its direct case, therefore a corresponding adjustment is necessary to properly synchronize with the accumulated deferred income taxes.
[9] Multer Rebuttal Testimony at 7.

Company has updated its base period and forecast period revenue requirement to remove various deferred tax items from rate base related identified by the OAG.[10]

2. Contested Issues Between the Parties

a. It is acceptable to adjust DTA NOL ADIT through the end of the base period.

As noted in the rebuttal testimony of Company witness Multer, the Company disagrees with Mr. Kollen's methodological assumption that there would be a further reduction to the Company's asset NOL ADIT for the April through December period at the same rate as was experienced in the first six months of the base period.[11] Mr. Kollen's underlying assumption and therefore his proposal are not reasonable as the Company's test year projections were valid estimates at the time of filing in this proceeding as evidenced by the Company's actual results for the period April 1, 2021 through September 30, 2021 (the Company's most recent fiscal year-end) as well as the Company's historic results and deferred tax assumptions for the test period (calendar year 2022).[12]

b. The Inclusion of Accounts Payable Related to Construction Is Appropriate and Consistent with Prior Cases.

As noted in the direct and rebuttal testimony of Company witness Christian, the Company has followed the same methodologies as was filed and approved in Case Nos. 2017-00349 and 2018-00281 as filed, despite items in the study being litigated by Mr. Kollen. He now introduces a new methodology that has not been included in the Company's previous lead/lag studies that results in a lowering of our requested rate base related to working capital. One of the purposes of doing so is a good faith attempt to minimize disagreement and controversy by maintaining a consistent approach

[10] Christian Rebuttal Testimony, Exhibit JTC-R-1.
[11] Multer Rebuttal Testimony at 8.
[12] *Id.* at 8-9. The base period experienced a net reduction of the asset NOL ADIT of $36.3 million ($71.1 million for six months, less an increase of $34.9 million for the last six months) over the full period compared to Mr. Kollen's proposed additional reduction of $71.1 million for the last six months.

that has been found to be just and reasonable. Mr. Kollen, however, chose to pick one methodological item in the cash working capital calculation to dispute in order to lower the requested rate base related to working capital. While Mr. Kollen does cite to a similar adjustment being accepted by the Commission in Case No. 2020-00174 and in a settlement by another utility, he does not provide a reason why this adjustment is warranted and necessary for Atmos Energy. This introduction of a new approach to a single issue within determination of cash working capital undermines the purpose of basing a filing on prior positions of the OAG and this Commission's prior orders when preparing this case.

c. The Company's Inclusion of a Regulatory Asset Related to Rate Case Expense is Appropriate and Consistent with Prior Cases.

The OAG's rationale for excluding this rate base item is unreasonable. First, the Company's inclusion of a regulatory asset related to rate case expense is consistent with our previous cases. Despite the prior approval, Mr. Kollen argues that the customer does not receive a benefit from the regulatory asset. The very strong implication is that customers do not benefit from just and reasonable rates, which is incorrect. These are unavoidable costs to serve our customers made necessary by the laws of Kentucky and the rules and orders of this Commission so that Atmos Energy can recover its costs and an opportunity to earn a reasonable return.

Next, Mr. Kollen suggests that the shareholder will benefit from a declining balance as the asset amortizes. However, he neglects to mention that many, if not all, of the Company's other rate base items change balances after the test period end, including continued capital investments that can only be included in customer rates after a full rate case proceeding (non-PRP expenditures). Thus, by definition (to use his term) the Company will not recover these assets that are not included in rate base after the end of the test period. His concerns over the regulatory asset related to rate case expenses

are misplaced.[13]

d. The Methodology Used for Cash Working Capital by Atmos Energy Is Appropriate and Should Not Be Adjusted.

As noted in the direct and rebuttal testimony of Company witness Christian, the Company has followed the same methodologies as was filed and approved in Case Nos. 2017-00349 and 2018-00281 as filed. In this case, the OAG introduced a new methodology that has not been included in the Company's previous lead/lag studies that results in a lowering of our requested rate base related to working capital. The OAG has provided no substantive evidence to support the suggested change. There is no reason to accept this change.

B. Operating Income Issues

1. Areas of No Disagreement Among the Parties

a. The Company Agrees with the OAG's Adjustment to Rate Case Expense.

2. Areas of Disagreement Among the Parties.

a. The Outside Services Expense Included in this Case Is Appropriate.

Mr. Kollen has selected one category out of our overall expenses to propose an adjustment. A more reasonable approach is to look at the overall O&M to include both budget categories that are higher and lower, not just one item that is higher by historical standards as Mr. Kollen's methodology relies upon. Exhibit JTC-R-5 compares the overall O&M in the base period "as filed" of $31.312 million to the actual base period amount of $32.015 million or 2.25% higher than anticipated. Excluding bad debt expense, the variance was .42% lower than anticipated. Atmos Energy monitors and manages its overall O&M budget, anticipating that some specific categories, such as Outside Services, may fall above or below expected levels and adjusting accordingly. A more reasonable approach is to look at the overall O&M in order to include both budget categories that are higher and

[13] Christian Rebuttal Testimony at 25.

lower, not just one item that is higher by historical standards as Mr. Kollen's methodology relies upon.

b. Atmos Energy's Proposed Bad Debt Tracker Is in the Public Interest and Should Be Approved.

Establishment of a regulatory asset would avoid both an over and under recovery of bad debt expense that is resulting from the uncertainty of COVID-19. The Company did not reinstitute dunning procedures in Kentucky until June 2, 2021, and began by prioritizing higher outstanding amounts due.[14] The ability to forecast a reasonable amount of bad debt expense is hindered and thus a tracker mechanism is proposed to balance the needs of the customer and the Company. Mr. Kollen misinterprets our response in discovery regarding this issue and incorrectly suggests that establishing the Company's proposed regulatory asset for bad debt expense would "overlay another deferral mechanism when one already exists." We state in the response that the accounting is for GAAP purposes and go on to describe how it is recorded on the books and records of the Company. The response then goes on to explain the regulatory asset proposal and how it would interact with our GAAP expense but does not suggest that our recovery in this case is based on the higher than ordinary "per book" expense currently being experienced due to the COVID-19 Pandemic. When asked in discovery if his recommendation was to therefore use FERC account 9040 per books as our basis for bad debt expense (GAAP) in this case, he rejected the suggestion stating that he recommended no changes to our requested expense. His response indicates a disconnect between his understanding of what we have included in our revenue requirement for bad debt expense and what is recorded for GAAP purposes. [15]

Finally, the four criteria under which the Commission approves establishing a regulatory asset are: (1) an extraordinary, nonrecurring expense which could not have reasonably been anticipated or included in the utility's planning; (2) an expense resulting from a statutory or administrative directive;

[14] Atmos Energy's Response to Staff's Sixth Request, Item 6.
[15] Christian Rebuttal Testimony at 32; *see also* OAG's Response to Atmos Energy's First Request, Item 8.

(3) an expense in relation to an industry-sponsored initiative; or (4) an extraordinary or nonrecurring expense that over time will result in a saving that fully offsets the cost. The Bad Debt Tracker is in the public interest because it addresses extraordinary, nonrecurring expense which could not be reasonably anticipated or included in the utilities planning and the expense results from a statutory or administrative directive.

C. Cost of Capital Issues

1. Atmos Energy's Rates in Kentucky Should Reflect the Company's Actual Capital Structure.

In recent years, the landscape of the natural gas distribution industry has changed substantially, with new technologies, changing customer needs, and challenges from increasingly stringent safety regulations. The goal of the regulation of pipeline safety in the natural gas industry is to set operational standards that advance the safe transportation and delivery of natural gas to each utility's customers. New rules have been enacted on federal and state levels to guide natural gas distribution companies accelerating the replacement and modernization of their distribution system. Atmos Energy in conjunction with the Commission has taken the steps necessary to adjust to this new landscape, expanding its capital investment in safety while continuously enhancing its customer service and maintaining affordable rates.[16] A key issue is whether the past steps taken by Atmos Energy and the prior decisions of the Commission related to capital spending in safety and other infrastructure remain sufficient given the changes that have occurred since the last rate case and will continue to occur into the foreseeable future.

As noted above, utility's rates must provide enough revenue to cover its operating expenses and **the cost of capital**. Federal Power Comm'n v. Hope Natural Gas Co., 320 U.S. 591 (1944). As our own Kentucky high court has stated, when establishing rates, the Commission must ensure the

[16] Christian Rebuttal Testimony at 8-9.

resulting rates will, inter alia, "…enable the utility to operate successfully, to maintain its financial integrity [and] to attract capital." Commonwealth ex rel Stephens v. South Central Bell Telephone Co., 545 S.W.2d 927, 930-31 (Ky. 1976). To maintain the financial health necessary to undertake the necessary level of capital investments in the recent past in in the upcoming years, the Atmos Energy management team made the decision to strengthen and maintain the Company's balance sheet by incorporating a higher level of equity in its capital structure for the benefit of both its customers and its owners.[17] Atmos Energy's long-term business strategy has enhanced the safety of our customers.

Atmos Energy's organizational structure is unique among its peers both nationally and within the Commonwealth of Kentucky. Among both its peer group used in the ROE calculations in this docket and the other investor-owned utilities in Kentucky, Atmos Energy is the only utility that is not structured as a parent or holding company with subsidiary utilities. The Kentucky division, along with each of the other unincorporated divisions, are part of the legal entity that is Atmos Energy Corporation. Therefore, all debt or equity funding of the operations performed by the utility divisions must be (and is) issued by Atmos Energy as a whole, on a consolidated basis. In other words, while utilities like Duke-Kentucky and Columbia Gas have markedly different capital structures at the holding company level (with typically lower equity ratios) than at the operating company level which produces a higher effective ROE at the holding company level, Atmos Energy's one consolidated balance sheet provides transparency that the ROE awarded by this Commission is the effective ROE received.[18] For this and other reasons that make Atmos Energy unique, the capital structure necessary for this period of accelerating investment may vary from that of its peers.[19]

It is also unrefuted that this management strategy is working to the benefit of Atmos Energy's Kentucky customers. Atmos Energy has maintained financial and operational stability during

[17] Christian Direct Testimony at 57-58; For treatise support of the deference given to managerial judgment, see Christian Rebuttal Testimony at 20, citing R. Morin, New Regulatory Finance, at p. 470.
[18] Christian Rebuttal Testimony at 19-21.
[19] Christian Direct Testimony at 62.

unprecedented events such as the COVID-19 pandemic, the February 2021 winter event, the implementation of the Tax Cuts and Jobs Act,[20] and the recent tornadoes in the Southeast whose devastation hit Atmos Energy's service territory in Kentucky.[21] During all of these periods of uncertainty and challenge, Atmos Energy has continued to make investments in the long-term safety of its pipeline system in Kentucky, working closely with the Pipeline Safety Division of this Commission. Meanwhile Atmos Energy's distribution charges, particularly for residential customers, are the lowest among the major utilities in Kentucky with pass-through gas costs among the lowest in the state.[22]

While the OAG has recommended rejection of the use of the actual capital structure, he has failed to provide any substantive evidence to discredit its use. Relying only on differences in opinion of its witnesses, he has not introduced any facts to warrant the Commission disregarding the actual capital structure. The OAG does not put forth evidence that the management of Atmos Energy has made unsound or imprudent decisions regarding financing the capital used to invest in its system for the benefit of its customers. The only facts put forth by the OAG in support of its recommended imputation of a hypothetical capital structure are the equity ratios of other utilities. Without proof of unreasonableness or imprudent management, the use of the actual capital structure should be allowed.[23]

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[20] Christian Rebuttal Testimony at 12.
[21] Christian Direct Testimony at 58-59.
[22] Taylor Direct Testimony at 11; Atmos Energy Response to Staff's Second Request, Item 6.
[23] *See, e.g., State of Mississippi ex rel. Pittman v. Miss. Public Serv. Comm'n.*, 538 So.2d 387 (Miss. 1989); *Southern Bell Tel. & Tel. v. Mississippi Public Serv. Comm'n.*, 113 So.2d 622 (Miss. 1959) (allowing imputation of hypothetical capital structure by PSC only upon proof that the capital structure of the company was "imprudent and uneconomical"); *People's Natural Gas Div. v. Public Utilities Comm'n.*, 567 P.2d 377, 379 (Colo. 1977) ("A guiding principle of utility regulation is that management is to be left free to exercise its judgment regarding the time of entering financial markets and its judgment regarding the most appropriate ratio between debt and equity in the capital structure."); *Continental Tel. Co. v. Alabama Public Serv. Comm'n*, 376 So.2d 1358, 1365 (Ala. 1979) ("It is also incorrect to arbitrarily disregard capital ratios absent some showing in the record that the ratios are temporarily distorted, deliberately misstated, or otherwise unreliable."); *Turpen v. Oklahoma Corp. Comm'n.*, 769 P.2d 1309, 1330 (Okla.1988) ("Since good faith is presumed on the part of public utility managers, their judgment about prudent outlays, including outlays for capital, should not be overruled unless inefficiency or improvidence on their part is shown"); *South Cent. Bell Telephone Co. v. Louisiana Public Serv. Comm'n.*, 594 So.2d 357 (La. 1992) (holding that, "there having been no finding…that the actual capital structure of the utility resulted from unreasonable or imprudent investments," a utility was "entitled to have its rates fixed on the basis of its actual cost of capital under its existing capital structure"); *Boise Water Corp. v. Idaho Pub. Util. Comm'n*, 555 P.2d 163, 173 (Idaho 1976) (holding that regulator must accept for ratemaking purposes the actual capital structure of the utility unless it finds, on the basis of substantial evidence, that the structure is unreasonably

In contrast to the OAG witnesses, the testimonies of Joe Christian and Dylan D'Ascendis describe in detail the benefit and necessity of an actual capital structure. It is without question that now is a time of capital expansion for utilities, and Atmos Energy has positioned itself to have sufficient access to the capital markets at a reasonable cost, assuming supportive regulatory treatment.[24]

Mr. D'Ascendis's testimony explains the rationale and policy that support the appropriateness of setting rates based upon the utility's actual capital structure, the reasonableness of Atmos Energy's capital structure, and the relationship between credit metrics and ratings and the cost of capital.[25] Mr. Christian's testimony provides further detail regarding Atmos Energy's credit rating, the factors analyzed by the credit rating agencies to determine Atmos Energy's credit outlook and the relationship between Atmos Energy's level of long-term debt and its Key Financial Indicators ("KFI's"), which are crucial factors that determine the Company's credit outlook. Mr. Christian also quantifies the cost to its customers of deteriorating KFI's that would result from increasing the level of debt financing.[26]

Atmos Energy notes that the OAG has attempted to characterize the capital structure used by Atmos Energy as a "hypothetical" capital structure as well, since it is applied to a future test period. This is a false assertion. An "actual" or expected capital structure in cases of future test periods, just like any other forecasted costs based on historical information, is one that is based on historical, actual data and fairly represents the expectations of the capital structure for the test period.[27] It is a capital structure that will actually allow the utility to recover its costs of capital during the forecasted period, as required by Federal Power Comm'n v. Hope Natural Gas Co. This is in stark contrast to the hypothetical capital structure recommended by the OAG, which arbitrarily imputes a capital structure with a much lower equity ratio than any experienced by Atmos Energy in the recent past or forecasted

constructed).
[24] Christian Rebuttal Testimony at 13-15.
[25] D'Ascendis Rebuttal Testimony at 54-60.
[26] Christian Rebuttal Testimony at 10-11.
[27] C. Phillips, The Regulation of Public Utilities, 388 (1993).

for the future and that would disallow recovery of capital costs that Atmos Energy will incur with reasonable certainty during the test period.

2. Return on Equity

It is important that the authorized return on equity "ROE" reflects the risks and prospects of the utility's operations and supports the utility's financial integrity from a stand-alone perspective as measured by their combined business and financial risks. Consequently, the ROE authorized in this proceeding should be sufficient to support the operational (*i.e.,* business risk) and financing (*i.e.,* financial risk) of the Company's Kentucky utility operations on a stand-alone basis.

Business risks generally faced by utilities include but are not limited to the regulatory environment, mandatory environmental compliance requirements, customer mix and concentration of customers, service territory economic growth, market demand, risks and uncertainties of supply, operations, capital intensity, size, the degree of operating leverage, and the like, all of which have a direct bearing on earnings.

Financial risk is the additional risk created by the introduction of debt and preferred stock into the capital structure. The higher the proportion of debt and preferred stock in the capital structure, the higher the financial risk to common equity owners (*i.e.,* failure to receive dividends due to default or other covenants). Therefore, consistent with the basic financial principle of risk and return, common equity investors demand higher returns as compensation for bearing higher financial risk.[28]

The models used by Mr. D'Ascendis are all market based. The Discounted Cash Flow ("DCF") model uses market prices in developing the model's dividend yield component. The Risk Premium Method ("RPM") uses bond ratings and expected bond yields that reflect the market's assessment of bond/credit risk. In addition, beta coefficients (β), which reflect the market/systematic risk component of equity risk premium, are derived from regression analyses of market prices. The Predictive Risk

[28] D'Ascendis Direct Testimony at 10-11.

Premium Model ("PRPM") uses monthly market returns in addition to expectations of the risk-free rate. The Capital Asset Pricing Model ("CAPM") is market based for many of the same reasons that the RPM is market based (*i.e.*, the use of expected bond yields and betas). Selection criteria for comparable risk non-price regulated companies are based on regression analyses of market prices and reflect the market's assessment of total risk.[29] Relying on the DCF model, the RPM, and the CAPM, applied to the Utility Proxy Group is appropriate because reasonable investors use a variety of tools and do not rely exclusively on a single source of information or single model. Moreover, the models on which he relies focus on different aspects of return requirements and provide different insights to investors' views of risk and return.

The DCF model, for example, estimates the investor-required return assuming a constant expected dividend yield and growth rate in perpetuity, while Risk Premium-based methods (*i.e.,* the RPM and CAPM approaches) provide the ability to reflect investors' views of risk, future market returns, and the relationship between interest rates and the cost of common equity. Just as the use of market data for the Utility Proxy Group adds the reliability necessary to inform expert judgment in arriving at a recommended common equity cost rate, the use of multiple generally accepted common equity cost rate models also adds reliability and accuracy when arriving at a recommended common equity cost rate.[30]

He also used multiple cost of common equity models as primary tools in arriving at his recommended common equity cost rate, because no single model is so inherently precise that it can be relied on to the exclusion of other theoretically sound models. Using multiple models adds reliability to the estimated common equity cost rate, with the prudence of using multiple cost of common equity models supported in both the financial literature and regulatory precedent.[31]

[29] *Id.* at 13.
[30] *Id.* at 15-16.
[31] *Id.* at 42.

Atmos Energy has greater relative risk than the average utility in the Utility Proxy Group because of its smaller size compared with the utilities in that group, as measured by an estimated market capitalization of common equity for Atmos Energy. Atmos Energy's estimated market capitalization was $597.101 million as of May 28, 2021, compared with the market capitalization of the average company in the Utility Proxy Group of $4.6 billion as of May 28, 2021. The average company in the Utility Proxy Group has a market capitalization 7.7 times the size of Atmos Energy's estimated market capitalization. As a result, it is necessary to upwardly adjust the range of indicated common equity cost rates between 9.44% to 12.42% to reflect Atmos Energy's greater risk due to their smaller relative size.[32]

Flotation costs have been included in the calculation. They are those costs associated with the sale of new issuances of common stock. They include market pressure and the mandatory unavoidable costs of issuance (*e.g.*, underwriting fees and out-of-pocket costs for printing, legal, registration, etc.). For every dollar raised through debt or equity offerings, the Company receives less than one full dollar in financing. It is important to include these costs because there is no other mechanism in the ratemaking paradigm through which such costs can be recognized and recovered. Because these costs are real, necessary, and legitimate, recovery of these costs should be permitted. As noted by Morin:

> The costs of issuing these securities are just as real as operating and maintenance expenses or costs incurred to build utility plants, and fair regulatory treatment must permit recovery of these costs…. The simple fact of the matter is that common equity capital is not free….[Flotation costs] must be recovered through a rate of return adjustment. (D'Ascendis Direct p. 48)

Mr. D'Ascendis' recommendation results from applying several cost of common equity models, specifically the Discounted Cash Flow ("DCF") model, the Risk Premium Model ("RPM"), and the Capital Asset Pricing Model ("CAPM"), to the market data of a proxy group of seven natural gas distribution utilities ("Utility Proxy Group") whose selection criteria will be discussed below. In

[32] *Id.* at 45-46.

addition, he applied the DCF model, RPM, and CAPM to a proxy group of 48 domestic, non-price regulated companies comparable in total risk to the Utility Proxy Group ("Non-Price Regulated Proxy Group").

In contrast to the multi-layered analysis of Mr. D'Ascendis, the OAG's witness Mr. Baudino, has provided an incomplete, inaccurate study. Mr. Baudino recommends an ROE range of 8.40% to 9.40%, with a point estimate of 9.10%, based exclusively on the results of his Constant Growth DCF analyses applied to his proxy group of seven natural gas utilities. Mr. Baudino also performs two CAPM analyses, although he does not give those results weight in arriving at his ROE recommendation.[33] Mr. Baudino relies exclusively on his constant growth DCF model results to determine his recommended ROE. Mr. D'Ascendis provides detailed support for the use of multiple models on pages 4 and 5 of his rebuttal testimony. He also noted that he found no literature supporting Mr. Baudino's use of projected DPS growth rates for use in a DCF model.[34]

There are also problems with Mr. Baudino's CAPM analysis. Mr. Baudino's CAPM analysis is flawed in at least three respects. First, he has incorrectly relied on a historical, *i.e.*, recent, six-month average 30-year Treasury bond yield as his risk-free rate. Even though Mr. Baudino exclusively relies on projected growth rates in his DCF analyses, noting that growth in the DCF is expected, he fails to apply that logic to selecting an appropriate interest rate in his CAPM analysis. Using projected interest rates in his CAPM analysis would be consistent with his above statement and its application of his DCF model. Current interest rates are not proven to be a better predictor of future interest rates. Equity securities represent a perpetual claim on cash flows; 30-year Treasury bonds are the longest-maturity securities available to approximate that perpetual claim. Thus, Mr. Baudino's use of a 20-year

[33] Baudino Direct Testimony at 3.
[34] D'Ascendis Rebuttal Testimony at 18.

Treasury bond yield does not match the life of the assets being valued. The use of a 30-year Treasury bond yield is a more appropriate risk-free rate.[35]

Second, he fails to consider several approaches supported by his own testimony in this proceeding and in other proceedings in calculating the MRP. His MRP mismatches a projected return on the market with a historical bond yield. A more correct way to derive that MRP would be to use the projected return and subtract a projected risk-free rate. The method he used in this case differs from that used in other regulatory proceedings.[36]

Third, Mr. Baudino did not incorporate an empirical CAPM ("ECAPM") analysis even though empirical evidence indicates that low-beta securities, such as utilities, earn returns higher than the CAPM predicts and high-beta securities earn less.[37]

The results of the corrections to Mr. Baudino's DCF model and CAPM are provided in the table below:

Summary of Baudino Corrected Results

Measure	Method 1	Method 2
Discounted Cash Flow Model	9.85%	9.58%
	CAPM	**ECAPM**
Capital Asset Pricing Model	9.94%	10.14%

In view of these corrected results, Mr. Baudino's reasonable range of ROEs would be from 9.58% to 10.14%. However, an indicated range of ROEs from 9.58% to 10.14% still understates Atmos Energy's ROE because it does not reflect its relative risks to the proxy group and flotation costs.[38] Adjusting for flotation costs in Mr. Baudino's calculations results in the following:

Summary of Baudino Corrected Results with Adjustments

Measure	Method 2
Indicated Range of ROEs Before Adjustment	9.58% - 10.14%
Business Risk Adjustment	0.20%

[35] *Id.* at 26-27.
[36] *Id.* at 28-29.
[37] *Id.* at 23-24.
[38] *Id.* at 34-35.

Credit Risk Adjustment	-0.08%
Flotation Cost Adjustment	0.06%
Indicated Range of ROEs After Adjustment	9.76% - 10.32%

In view of these corrected and adjusted model results, Mr. Baudino's initial range of ROEs from 8.40% to 9.40% significantly understates the ROE for Atmos Energy at this time.[39]

Next, Mr. Baudino claims that there is no consensus regarding the use of a size premium for utilities. Duff & Phelps' ("D&P") 2020 Cost of Capital: Annual U.S. Guidance and Examples Market Results Through 2019 ("D&P 2020") presents a Size Study based on the relationship of various measures of size and return: "The size of a company is one of the most important risk elements to consider when developing cost of equity estimates for use in valuing a firm."[40] As company size decreases (increasing size rank), the Coefficient of Variation "CoV" increases, linking size and risk for utilities, which is significant at 95.00% confidence level. This is important because the Commission should assess Atmos Energy as a stand-alone company because it is Atmos Energy's rate base to which the overall rates of return set forth in this proceeding will be applied**.** In this proceeding, the property employed "for the convenience of the public" is the Kentucky jurisdictional rate base of Atmos Energy. Thus, it is only the risk of investment in Atmos Energy that is relevant to the determination of the cost of common equity to be applied to the common equity-financed portion of that rate base.[41]

Considering the detailed, annotated analysis of the appropriate ROE by Mr. D'Ascendis, and the limited, one model analysis of Mr. Baudino, the credible evidence is undisputable and Mr. D'Ascendis recommendation as updated to reflect the current market situation should be adopted.

In his rebuttal testimony, Mr. D'Ascendis updated his ROE analyses as of September 30, 2021. Based on these updated analyses, the range of reasonable ROEs attributable to Atmos Energy is between 9.76% and 12.88% (unadjusted) and 9.94% to 13.17% (adjusted). In view of the unadjusted

[39] D'Ascendis Direct Testimony at 42.
[40] D'Ascendis Rebuttal Testimony at 36.
[41] *Id.* at 40-41.

and adjusted ranges of ROE, the original ROE recommendation of 10.35%, which is in the bottom half of the range of ROEs, it is a conservative measure of the Company's ROE at this time. Therefore, the specific ROE recommendation of 10.35% for Atmos Energy in this case continues to be reasonable.

Using data available as of September 30, 2021, the updated results are presented in Table 1, below.

Table 1: Updated Cost of Common Equity Results

Discounted Cash Flow Model	9.76%
Risk Premium Model	10.30%
Capital Asset Pricing Model	12.10%
Cost of Equity Models Applied to Comparable Risk, Non-Price Regulated Companies	12.99%
Indicated Range	9.76% - 12.99%
Size Adjustment	0.20%
Credit Risk Adjustment	-0.08%
Flotation Cost Adjustment	0.06%
Recommended Range	9.94% - 13.17%
Recommended Cost of Common Equity	10.35%

D. Pipeline Replacement Rider Issues

1. Atmos Energy's Proposal to Include Aldyl-A Projects in its PRP Is Appropriate, Consistent with Commission Precedent, and in the Public Interest.

Atmos Energy continuously strives to improve the safety and reliability of its pipeline system. Vital steps in this process include (1) proactively identifying assets where the risk of

failure is high and then (2) designing and implementing a plan to mitigate those risks. Through that process, Atmos Energy has identified a need to continue its Pipeline Replacement Program ("PRP") in Kentucky and modify that program to include projects that target a certain type and generation of polyethylene ("PE") pipe known as Aldyl-A, in addition to the bare steel pipe that is already the focus of our program.[42] Accelerated replacement of this aging pipeline infrastructure is necessary to continue to maintain the safety and reliability of the system, given the increasing risk of leakage posed by this pipe. The Company believes that its Pipeline Replacement Program ("PRP") continues to be an appropriate means to manage and fund the necessary investments to update Atmos Energy's gas distribution system and to help ensure the system remains safe and reliable for customers over the long term.

Atmos Energy's Kentucky system has approximately 118 miles remaining of bare steel pipe in its system, most of which has been in place since before the 1960s. In addition, of the early generation plastic pipe in Atmos Energy's Kentucky system, there are approximately 205 miles of Aldyl-A. The natural gas industry has determined that these materials are no longer appropriate for use in the construction of natural gas distribution systems. Bare steel and early generation plastic pipes deteriorate with age and are prone to leaks, which impacts both the safety and reliability of the pipeline system.[43]

Atmos Energy is subject to the PHMSA rules and regulations as those are promulgated by the U.S. Department of Transportation ("DOT") and adopted by the Commission for Kentucky natural gas local distribution companies.[44] The pipeline safety regulations provide the minimum that should be done to construct, operate, and maintain a natural gas system, which serves as a framework in which

[42] Austin Direct Testimony at 1.
[43] *Id.* at 2.
[44] *Id.* at 6.

operators must use their discretion to implement those standards in a manner that maximizes safety on its system given the constraints inherent in the process.[45]

Each operator is required to develop and implement its own unique Distribution Integrity Management Plan ("DIMP") to mitigate risks on its system. For example, Part 192.1007(c) requires the operator to evaluate and rank risk:

> "An operator must evaluate the risks associated with its distribution pipeline. In this evaluation, the operator must determine the relative importance of each threat and estimate and rank the risks posed to its pipeline. This evaluation must consider each applicable current and potential threat, the likelihood of failure associated with each threat, and the potential consequences of such a failure."

In this way, the regulation leaves to the operator the decisions of the factors and methodology that should be used to identify and address risk and the pace at which such identified risks should be addressed.[46]

Part 192 Subpart P regulations, every distribution operator is required to have a Distribution Integrity Management Program plan in place. The seven key elements of a DIMP plan are:

1. Knowledge of distribution system
2. Identify threats
3. Evaluate relative risk
4. Identify and implement measures to reduce risk
5. Measure performance, monitor results, and evaluate effectiveness
6. Periodic evaluation and improvement
7. Report results

Through the DIM process, assets on the Kentucky system have been identified as relatively high risk and sequenced for replacement, including bare steel, low pressure, and Aldyl-A assets.[47] In the most recent DIM model risk-ranking, material failures were identified as being a high risk in

[45] *Id.* at 6.
[46] *Id.* at 9.
[47] Austin Direct Testimony at 8; Atmos Energy's Response to Staff's Second Request, Item 30.

Kentucky. Upon further review of these material failures, it was determined that Aldyl-A Plastic was contributing to these high risks. This determination is supported by the leak rate tables provided in the Company's response to Staff DR No. 2-31 subpart (b).[48]

Atmos Energy's intention is not only to repair identified leaks but also to identify pipes where the risks of leaks or failure are more prevalent and to then design and implement a plan to mitigate those risks. As a result, Atmos Energy is investing capital into its system at a much higher annual rate than it has historically done to address safety and integrity issues identified through the risk assessment process.[49]

Based on a new emphasis by the federal regulators to address pipeline safety, particularly Aldyl-A **enacted since the last Atmos Energy rate case,** Atmos Energy has intensified its efforts to replace Aldyl-A. On December 27, 2020, Congress signed into effect the Protecting our Infrastructure of Pipelines and Enhancing Safety Act of 2020 ("PIPES Act of 2020"), which outlines provisions intended to continue to enhance safety, increase transparency, and refine the existing rulemaking process. One provision was a directive for natural gas operators to within one year evaluate their existing plans and take into consideration measures which would contribute to public safety and protect the environment. In advisory bulletin ADB-2021-01 dated June 4, 2021, PHMSA outlined its intention to begin performing inspections in 2022 on the adequacy of operators updated plans to meet the intent of Section 114 of the PIPES Act of 2020, including the requirement that "**Operators must also revise their plans to address the replacement or remediation of pipeline facilities that are known to leak based on their material, design, or past operating and maintenance history."**[50]

[48] Atmos Energy's Response to Staff's Second Request, Item 30.
[49] Austin Direct Testimony at 9.
[50] *Id.*, Exhibit TRA-1.

This requirement reinforces Atmos Energy's proactive assessment of existing Aldyl-A piping and the need to immediately begin replacement.[51]

Utilizing the PRP, Atmos Energy is proposing to continue to emphasize and complete replacement projects using a combination of risk analysis, industry-identified risk information, and input from its operational leadership whereby it can analyze, prioritize, and sequence the accelerated replacement based on the most crucial factors that impact customers and the community. In its PRP filing, the Company submits each project, project description, services and estimated costs by mains, service and meters where the Commission can have full transparency to review, issue discovery, and approve proposed projects before they begin.[52]

The PRP has enabled the Company to begin a systematic, long-term strategy of expediting the replacement of older and no longer industry-standard materials with safer, modern piping materials installed to current industry specifications. The Company's replacement of bare steel pipe is not complete. However, it has progressed pursuant to the schedule set by the Commission's Order in Case No. 2017-00349. As the Commission stated, "the original 15-year PRP time period should be extended and that annual ratepayer-funded PRP investment should be limited to $28 million, barring the identification of a PRP eligible pipeline-related hazard that could not have been reasonably foreseen. $28 million in annual investment should cause the remaining PRP for bare steel replacement to be complete in 6 - 7 years with estimated completion in 2027, adding two years to the originally approved 15-year timeframe."[53]

Based on the Commission's decision in Case No. 2017-00349, except for certain specific projects that were included in the past, the Commission considered the scope of the PRP to be solely to address the accelerated replacement of natural gas systems containing bare steel and related

[51] Austin Direct Testimony at 10-11; *see also* Austin Direct Testimony, Exhibit TRA-1.
[52] Austin Direct Testimony at 3.
[53] Case No. 2017-00349, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates and Tariff Modifications* (Ky. PSC May 3, 2018), Order at 41.

infrastructure. While the industry recognizes bare steel as one of the leading risk types, utilities need to have appropriate replacement cycles for all their pipeline infrastructure. The Company's approach is in line with the Commission's guidance from the Company's last final order in Case No. 2018-00281 indicating the reasons for support of an Aldyl-A replacement program for Delta Natural Gas Company. Specifically, the Commission highlighted the fact that Delta Natural Gas Company, Inc. acknowledged that all Aldyl-A did not need to be replaced immediately, but indicated that it had identified specific sections of Aldyl-A that should be targeted for replacement first, and then anticipating the remainder to be replaced over the course of several years. The Company's proposed Aldyl-A replacement in this Case is no different.[54] Atmos Energy has approximately 4,300 miles of distribution and transmission pipelines in Kentucky. If forty-three (43) miles (1%) of pipe is replaced each year, it would take 100 years to renew the system and then some of the segments would be 100 years old.

Reducing bare steel has reduced the occurrence of pipe failure and discovered leaks. Reducing leaks reduces risks to the public and enhances safety. As the following chart demonstrates, the rate of leaks in Kentucky has fallen steadily since the PRP began, which is strong evidence that the accelerated replacement has been effective thus far.[55]

Table TRA-1 – Number of Active Leak Orders on Kentucky System in January of Each Year

Date	# Leaks
Jan, 2011	1,127
Jan, 2012	1,308
Jan, 2013	1,354
Jan, 2014	1,169
Jan, 2015	1,076
Jan, 2016	677
Jan, 2017	600
Jan, 2018	489
Jan, 2019	405

[54] Austin Direct Testimony at 12.
[55] *Id.* at 17-18.

Jan, 2020	313
Jan, 2021	230

The table below shows the leaks of bare steel and Aldyl-A[56]:

Leaks of Bare Steel and Aldyl-A:

Year	Total Miles	Below Ground Leaks	Below Leaks / 100 Miles
2016	3,977.2	749	18.83
2017	4,019.6	621	15.45
2018	4,062.4	652	16.05
2019	4,081.3	586	14.36
2020	4,161.0	587	14.11

Year	Total Miles Bare PRP	Below Ground Leaks	Below Leaks / 100 Miles
2016	264.4	121	45.76
2017	235.0	114	48.51
2018	202.6	104	51.33
2019	172.3	88	51.07
2020	142.6	68	47.69

Year	Total Miles Aldyl-A	Below Ground Leaks	Below Leaks / 100 Miles
2016	205.8	73	35.47
2017	205.8	54	26.24
2018	205.8	65	31.58
2019	205.8	62	30.13
2020	205.8	56	27.21

Aldyl-A material failures have resulted in leaks that occur on the body of pipe, at the joint, and on the tapping tee. The industry has identified vintage Aldyl-A pipe as having heightened potential to experience material failure by cracking or splitting. Atmos Energy Kentucky has experienced failures where Aldyl-A pipe was found to have cracked or split.[57] Within DIM, risk is calculated as the Likelihood of Failure multiplied by the Consequence of a Failure. The Likelihood of Failure is

[56] Atmos Energy's Response to Staff Second Request, Item 31.
[57] Atmos Energy's Response to Staff's Third Request, Item 17.

determined using the number of leak occurrences. A larger quantity of leaks is directly correlated with a higher Likelihood of Failure as reflected in the Leak Table cited above. Aldyl-A has a higher risk of failure per mile than other material types, excluding bare steel. Atmos Energy's Kentucky gas distribution system still contains approximately 205 miles of Aldyl-A pipe.

Over the past ten years, in Kentucky leaks on Aldyl-A within the system have averaged 35% higher per 100 miles of pipe than leaks on other types of PE pipe. When compared with leaks on coated steel, the rate is over 250% higher per 100 miles of pipe.[58] Replacement is the only remedy for these pipes. There is no remedial action that will reverse the brittle cracking of this early generation plastic pipe.[59]

Based on this new analysis of leak types and numbers available since the last rate case, Atmos Energy is requesting authority to amend its PRP tariff for inclusion of certain projects to begin the targeted replacement of Aldyl-A, in addition to the currently authorized bare steel. The amended PRP, if approved, will facilitate the complete retirement or replacement of the two material types posing the highest relative risk to safety and reliability based upon industry guidance and Atmos Energy's expertise and experience in Kentucky maintaining the safety and reliability of the Company's gas distribution system.[60]

Not all Aldyl-A will be replaced immediately. Contrary to the OAG's witness Mr. Kollen's assertion, it is not Atmos Energy's recommendation to replace *all* Aldyl-A pipe *immediately*, as that is not how the principles of Distribution Integrity Management ("DIM") work. Rather, the Aldyl-A sections are examined and prioritized in a comprehensive risk-based analysis using risk analysis tools, additional subject matter expert input, and other relevant data rather than arbitrarily excluding those projects from the pipeline replacement program simply because they are not bare steel. Such arbitrary

[58] Austin Direct Testimony at 26.
[59] *Id.* at 27.
[60] *Id.* at 21-22.

exclusion from a systematic relative-risk-based replacement program based on pipe material is not consistent with DIM principles.[61]

The prioritization of replacement accounts for factors such as age of material, location of the pipe in relation to population, and relative risk from third party damage. Based on consideration of these risk factors, the Company has identified specific sections of Aldyl-A that should be replaced immediately, and under its current proposal would anticipate the longer-term replacement of the remainder of Aldyl-A in its system by 2030. The Company proposes to incrementally add in Aldyl-A projects in FY22 in addition to its approximately $28 million of bare steel projects. At this rate, the estimated completion of the known Aldyl A would be by 2030.[62]

The Company would systematically decide which projects need to be prioritized in the early years of the program based on age of material, location of the pipe in relation to population, and relative risk from third party damage. Table TRA-4 below shows the age of the types of plastic pipe in Kentucky.[63]

Table TRA-4

Kentucky Aldyl-A System (in miles)	
Unknown Install Year	**33.5**
Pre 1973	**124.4**
1973 to 1983	**41.0**
Post 1983	**6.9**

The Company's Aldyl-A projects it is initially targeting for replacement are pre-1973 Aldyl-A pipe except for some smaller sections identified that warrant the replacement ahead of others due to additional risk factors or operational synergies. For example, there may be a small section of post-

[61] Austin Rebuttal Testimony at 6.
[62] Austin Direct Testimony at 28.
[63] *Id.* at 29.

1973 Aldyl-A pipe in the near vicinity of a project of older vintage already identified for replacement. While this newer section of Aldyl-A may not have been identified as a standalone project, it may be included because of the operational efficiencies of replacing it simultaneously with the adjacent sections and/or because there are risk factors other than age that influence the priority of the project, such as location in a highly populated or growing area with high probability of construction.[64]

The Company plans to include the additional Aldyl-A projects in its FY22 timeframe in addition to its projected $28 million of bare steel replacement. The costs of the incremental Aldyl-A projects for FY22 are currently projected at $2.79 million.[65] For FY23 the Aldyl-A projects are currently projected at $5.22 million.[66] The graph below lists each Aldyl-A project the Company would propose to do in FY22 and FY23:

Proposed Aldyl-A PRP Projects for Fiscal Year 2022

Project Name	Project Description
Aldyl.2635.Hillview Dr	Replace 2,176' of 2" PE, 2581' of 2" Aldyl A and 2,453' of 1.25" Aldyl A with 7,209' of 2" HDPE. 59 Services
Aldyl.2635.Sunset Circle	Replace 11' of 2" PE, 20' of 1.25" PE, 3,155' of 2" Aldyl A, and 2,585' of 1.25" Aldyl A with 5,777 of 2" HDPE. 70 Services
Aldyl.2635.Westend St	Replace 1,636' of 2" PE and 4,060' of 2" Aldyl A with 5,696' of 2" HDPE. 47 Services
Aldyl.2635.2nd St	Replace 149' of 1.25" PE, 1,340' of 2" Aldyl A, 1,488' of 1.25" Aldyl A, 1,145' of 2" PE, with 4,645' of 2" HDPE. 64 services

[64] *Id.* at 30.
[65] Atmos Energy's Response to OAG's First Request, Item 23.
[66] Atmos Energy's Response to OAG's First Request, Item 24.

Proposed Aldyl-A PRP Projects for Fiscal Year 2023

Project Name	Project Description
Aldyl.2636.KY 181	Replace 85' of 2" Fusion Bond Epoxy, 6,898' of 2" Aldyl A, 5' of unknown coating or size, 242' of 2" PE with 2" HDPE. 40 Services
Aldyl .2635.Lincoln Ave Cadiz	Replace 2,599' of 2" Aldyl A, 3,407' of 2" PE, 1,002' of 1" Aldyl A, with 7,008' of 2" HDPE. 53 services
Aldyl .2635.Lafayette St Cadiz	Replace 99' of 1.25" PE, 4,678' of 2" Aldyl A, 819' of 1.25' Aldyl A, 832' of 2" PE, 10' of unknown size or coating, 134' of 1" Aldyl A, with 6,579' of 2" HDPE. 54 services
Aldyl Monterey Rd	Replace 2,371' of 2" PE, 5,605' of 2" Aldyl A, with 7,975' of 2" HDPE. 65 services
Aldyl Spence Ln	Replace 1,212' of 2" PE, 2,634' of 2" Aldyl A, with 3,846' of 2" HDPE. 40 services
Aldyl.2734.Walnut St	Replace 101' of 1.25" Steel unknown coating, 3' of 1.25" PE, 3,054' of 2" Aldyl A, 5,682' of 1.25" Aldyl A, with 8,194' of 2" HDPE, 61 services
Aldyl.2734.N High St	Replace 5' of 2" PE, 4,249' of 2" Aldyl, 769' of 1.25" Aldyl A, with 5,023' of 2" HDPE. 70 services
Aldyl.2734.Fugate Ave	Replace 1,094' of 2" PE, 481' of 2" Aldyl A, 3,124' of 1.25" Aldyl A, with 4,699' of 2" HDPE. 41 services

Atmos Energy would not be able to make significant progress in the replacement of the Aldyl-A pipe in Kentucky if the replacement is not accelerated within PRP due to the current cap on non-PRP projects. Based on the current rate, the Company would replace all bare steel by 2028 at which

time pipeline replacement focus would shift to Aldyl-A. By expanding the PRP to include Aldyl-A the Company would start targeted replacement of Aldyl-A beginning in 2022 – six years earlier – and expect the life of the Aldyl-A replacement under PRP by 2030. Without the inclusion of Aldyl-A in its PRP it would be much more difficult to make a significant impact with current capital constraints and to replace Aldyl-A in the Company's system by the 2030 timeframe.[67]

In contrast to the Company's emphasis on the need to modify the PRP tariff based on safety concerns, the OAG's witness focuses exclusively on customer growth or cost savings. According the OAG's witness Mr. Kollen, including Aldyl-A pipe in the PRP is not prudent financially or operationally from a safety standpoint. Mr. Kollen's testimony contains an unsubstantiated disapproval of safety investment in Aldyl-A replacement on Atmos Energy's system, which is inconsistent with the OAG's position in the rate case of Columbia Gas of Kentucky, Inc., as discussed in the testimony of David Dittemore in Docket No. 2021-00183 filed on September 10, 2021. In that testimony, the OAG acknowledged that "the Company is in the best position to develop a rank-order of priorities for pipes to be replaced" and supported "giving the Company the discretion to prioritize pipe replacement based upon the results of its risk assessment." He further recommended "expanding the qualifying projects under [Columbia's pipeline replacement program] to include the costs of Aldyl-A replacements made under the Company's risk assessment results" while "requir[ing] the Company to establish the need for replacement by providing known leak rates, and any other objective criteria such as the results of in-line and other visual inspections of pipes the Company identifies for replacement.[68]

Contradicting the OAG's position in the Columbia case, Mr. Kollen also states that "it does not make sense to embark on an accelerated program to replace all of the Aldyl-A pipeline and further increase customer rates at least until after the accelerated bare steel replacement program is completed

[67] Austin Direct Testimony at 32.
[68] Austin Rebuttal Testimony at 3.

and then only after a comprehensive review." He also misstates the purpose of replacement that attempts to justify denial of safety-related capital investment because of forecasts of "minimal customer and usage growth."[69] Safety is not a growth-driven factor and is not relevant to the miles of pipeline replaced or the cost of replacement. The point of such alternative rate recovery mechanisms like the PRP is to facilitate pipeline replacement investment that is not associated with growth or increases in usage.[70] Mr. Kollen focuses solely on the minimization of rates at the expense of safety.

The underlying problem with the OAG's argument is that it fails to recognize that the fundamental purpose of infrastructure mechanisms like the Company's PRP is to enable utilities to accelerate replacement of aging infrastructure that poses potential safety and/or reliability concerns for customers. KRS 278.509 was enacted by the Kentucky legislature to enable utilities to accomplish these important objectives by allowing recovery of replacement investments outside of or between general rate cases. KRS 278.509 was clearly enacted to encourage these safety-related investment – not to discourage them.

The OAG's complaint with the PRP is that the Company has spent too much money in a global sense replacing aging and obsolete infrastructure. The OAG has not criticized the appropriateness of any particular project or the actual costs incurred for any project. The OAG just complains the Company has spent too much, while failing to mention the concept of safety in its PRP recommendation. Under KRS 278.509, the test for whether the costs incurred in PRP projects are recoverable is whether the costs incurred are fair, just and reasonable. The OAG's one-sided analysis of the Company's PRP has provided no evidence of any kind that disputes the costs incurred by Atmos Energy in its PRP to date are not fair, just and reasonable and, therefore, properly recoverable.

The Company was asked to explain why the more direct and rapid recovery of costs associated

[69] Kollen Direct Testimony at 43.
[70] Austin Rebuttal Testimony at 5.

with the PRP would not benefit Atmos by increasing the certainty of capital cost recovery and reducing regulatory lag and company risk. As noted in the Company's response to Staff DR No. 3-19, the Company's response to Staff's Second Request, Item 33 demonstrates that the risk associated with recovery of costs and capital in Atmos Energy's PRP is no more or less risky than the utility as a whole. Contrary to the premise of the question, there is no more direct or rapid recovery of costs associated with the PRP because the same depreciation lives associated with PRP investment are applicable to non-PRP investment. PRP costs are therefore recovered over the same life as non-PRP costs. The existence of a PRP tariff does provide a benefit to the Company through reduced lag and support of our credit health. The Company's response to Staff DR No. 3-19 subparts (a) and (c), illustrates that the commissions listed do not distinguish return outcomes based on type of recovery

There are benefits to the customer, including more rapid replacement of vintage infrastructure than would otherwise be possible (safe service), a lower cost of financing through better borrowing terms and avoidance of traditional rate case expenses (affordable service) and the ability to raise additional external capital to fund the PRP investments (the ability to continue receiving safe and reliable service). In other words, the PRP tariff follows a concept sometimes referred to as "the regulatory compact" by striking the appropriate balance between the customer and the Company. [71] There is no evidence in the record to support a reduction of ROE for PRP costs.

2. Atmos Energy's PRP Rider Should Not Be Modified to Address Reductions in Asset Net Operating Loss ADIT.

As noted in the rebuttal testimony of Company witness Multer, the amount of asset NOL ADIT included within the Kentucky rate division rate base and PRP Rider are appropriate and should not be adjusted.[72] The amount of asset NOL ADIT included in the Company PRP Rider properly reflects the

[71] Atmos Energy's Response to Staff Fourth Request, Item 5
[72] Multer Rebuttal Testimony at 10.

impact of rider revenue and investments on ADIT.[73] In other words, the methodology that exists with the PRP model for calculating the NOL ADIT asset appropriately reflects the impact of the rider revenue increase and investment during the period of the revenue deficiency calculation. Mr. Kollen's proposal is an attempt to incorporate changes in PRP occurring outside the PRP revenue requirement. As was previously discussed, the Company's methodology in this proceeding to calculate and account for changes in the NOL ADIT is the appropriate methodology for use in establishing base rates.

3. Spending Limits on Capital

The Company's capital spending has been restricted by the Commission in the Company's two prior rate cases. In Case No. 2017-00249 the Commission limited the Company's PRP spending to $28 million in annual investment for bare steel replacement only beginning in 2019 with an estimated completion in 2027.[74] The $28 million in annual investment was found to be reasonable by the Commission based on Atmos Energy's average actual annual PRP investment from 2012 through 2017.[75] In the Company's subsequent rate case, Case No. 2018-00281, the Commission restricted the Company's non-PRP capital spending in addition to the existing restriction on the Company's PRP capital spending. In that case, the Commission stated, *inter alia*, that Atmos Energy failed to demonstrate that the accelerated replacement of certain facilities such as Aldyl-A that the Company stated presented safety and reliability issues was justified.[76] The Commission ordered that projected capital spending on non-PRP projects should be limited to a 5-year 2014 through 2018 historical average of $29.26 million.[77] The Commission stated that if its total non-PRP capital spending exceeds the 5-year rolling average, Atmos Energy should scrutinize the justification for its projects closely and

[73] *Id.* at 11.
[74] Case No. 2017-00349, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates and Tariff Modifications* (Ky. PSC May 3, 2018), Order at 41.
[75] *Id.*
[76] Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 7, 2019), Order at 21.
[77] Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 7, 2019), Order at 24.

be prepared to provide documentation showing how each project is consistent with its DIMP or TIMP.[78]

The Company has agreed and committed to the Commission's timeline for bare steel replacement by 2027 at an approximate capital spending rate of $28 million per year. The Company has argued in this Case for removal of the restrictions on capital outside of bare steel investment for a variety of safety and public interest issues. The capital restriction language in Case No. 2018-00281 encompasses **all** categories of investment outside of the Company's bare steel projects associated with its current PRP. Inflationary pressures were already being experienced coming out of Case No. 2018-00281, and these inflationary pressures have been magnified in recent months because of COVID-19 restrictions, consumer behavior and economic factors.[79] The current limitations imposed by the Commission on the Company's non-PRP capital do not consider these factors, and as a result the Company is able to do less and less each year for non-bare steel projects (as well as bare steel projects) due to rising prices and the flexibility of the Company is significantly impaired. In addition, the limits on non-PRP capital constrains investment associated with economic development and growth. Without flexibility to invest in growth opportunities because of the current spending limit, the Company cannot address future growth opportunities and its additional revenue impact.[80] The Company does not have the flexibility in Kentucky to proactively and timely meet the growing needs of the industrial sector and the corresponding growing needs of the commercial and residential sectors that result from that expansion.[81]

Allowing recovery of Aldyl-A projects through the PRP would partially alleviate capital constrains on the non-PRP side but would not be a full solution.[82] For the Company to be allowed

[78] Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 7, 2019), Order at 21; *see also* Christian Rebuttal Testimony at 35.
[79] Christian Rebuttal Testimony at 35.
[80] *Id.* at 35.
[81] *Id.* at 35.
[82] Christian Rebuttal Testimony at 35-36; Austin Rebuttal Testimony at 9-10.

accelerated replacement of Aldyl-A on the non-PRP side of capital spending the incremental amount would need to be in addition to the currently imposed capital restriction, or other non-PRP capital projects which are also critical would have to be eliminated.[83] With non-PRP capital restrictions in place, the Company would still potentially have inadequate capital for non-PRP projects, such as a large industrial growth customer that would be looking to locate to the Commonwealth.[84] Two primary examples of service areas in Atmos Energy's territory that are outgrowing system capacity are Bowling Green and Shelbyville.[85] Both areas have potential for industrial projects that would bring investment and jobs to the regions. However, if Atmos Energy needed to make capital investment in the region to support that growth, the Company's budget would be limited by the cap on non-PRP spending, and there is a high probability that the investment would not be possible given necessary system maintenance and safety projects that would take precedence.[86] The non-PRP capital restrictions have a significant impact on future economic growth in Kentucky if the Company cannot install new or improve existing facilities to meet growth demand while also potentially jeopardizing the continued safety and reliability of the Company's system since the non-PRP capital limitation encompasses all of the Company's capital spending outside what the Company is allowed for bare steel replacement only in its current PRP rider.

The Company supplied, in response to FR_16(7)(b), our Kentucky direct capital budget for fiscal years 2023, 2024, and 2025. As an alternative to the current cap on non-PRP spending, the Commission could remove the existing cap language from the previous two cases related to PRP and non-PRP capital investment and require the Company, pending any changes in future rate cases and circumstances that cannot be reasonably anticipated, manage within its planned capital spending as outlined in response to FR_16(7)(b). This would align the Company's current assessment of capital

[83] Austin Rebuttal Testimony at 10.
[84] Christian Rebuttal Testimony at 35-36
[85] Austin Rebuttal Testimony at 15.
[86] *Id.* at 15.

investment needs with a cap on investment akin to what the Commission has ordered in these past cases.[87]

E. Tax Act Adjustment Factor Issues

The Company has proposed as part of its Case the TAAF Tariff. The TAAF is designed to account for and implement the effects of future Federal and/or Kentucky income tax changes, whether such changes reflect an increase or a decrease to the tax rate. The TAAF is the difference between the income tax expense included in the revenue requirement approved by the Commission in the Company's most recent base rate proceeding and the calculated income tax expense if the increase or decrease of the Federal and/or Kentucky income tax rate had been in effect during the test year after applying the gross conversion factor.[88] This proposed tariff provides for a timely reflection in rates of the correct tax rate so that customers are not paying higher or lower bills than necessary to accurately recover these pass-through costs. The OAG believes the TAAF Tariff is not necessary, as the Commission already has a means to address tax change impacts.[89] However, the OAG does not consider the effort that involves the current analysis. The TAAF Rider does not preclude the Commission from undertaking its own analysis and/or requiring additional filings. What the TAAF Rider does is promote efficiency by creating a mechanism through which future tax changes can flow. In the event the impacts of a tax change were non-controversial, the TAAF Rider would save the Commission the need of conducting a proceeding to review the impacts of a tax change and result in a faster implementation of the impacts of that tax change.[90] The TAAF Rider allows all parties to

[87] Christian Rebuttal Testimony at 37.
[88] Taylor Direct Testimony at 23.
[89] *See* Kollen Direct Testimony at 50.
[90] Multer Rebuttal Testimony at 12.

avoid the time and expense of conducting a proceeding to implement a known and measurable change.

F. Lobbying Expense

In Case No. 2018-00281 The Commission put Atmos Energy on notice that records related to lobbying expenses need to be filed with the next base rate case, at which time a determination will be made if any adjustment to employee salaries, taxes, and benefits is needed to reflect lobbying related activities.

As part of its response to the Commission's comment, Atmos Energy reviewed the definition of lobbying as defined in Ky. Rev. Stat. § 6.611(27), which states as follows:

> (a) "Lobby" means to promote, advocate, or oppose the passage, modification, defeat, or executive approval or veto of any legislation by direct communication with any member of the General Assembly, the Governor, the secretary of any cabinet listed in KRS 12.250, or any member of the staff of any of the officials listed in this paragraph.
> (b) "Lobbying" does not include:
> 1. Appearances before public meetings of the committees, subcommittees, task forces, and interim committees of the General Assembly;
> 2. News, editorial, and advertising statements published in newspapers, journals, or magazines, or broadcast over radio or television;
> 3. The gathering and furnishing of information and news by bona fide reporters, correspondents, or news bureaus to news media described in paragraph (b)2. of this subsection;
> 4. Publications primarily designed for, and distributed to, members of bona fide associations or charitable or fraternal nonprofit corporations;
> 5. Professional services in drafting bills or resolutions, preparing arguments on these bills or resolutions, or in advising clients and rendering opinions as to the construction and the effect of proposed or pending legislation, if the services are not otherwise connected with lobbying; or
> 6. The action of any person not engaged by an employer who has a direct interest in legislation, if the person, acting under Section 1 of the Kentucky Constitution, assembles together with other persons for their common good, petitions any official listed in this subsection for the redress of grievances, or other proper purposes.

Atmos Energy also considered the Commission's prohibition on the inclusion of "political advertising" in rates, which is defined in KAR 5:016 as advertising intended to influence "public opinion with respect to legislative, administrative, or electoral matters, or with respect to any controversial issue of public importance." After reviewing these definitions and the Commission's Orders related to this issue, Atmos Energy determined that any such services performed on behalf of Atmos Energy are performed by external contractors and are not performed by employees of Atmos Energy's Kentucky/Mid-States division. 100% of all external lobbying activities are coded to account 4264 and excluded from recovery.[91]

The three positions of Vice President of Rates and Regulatory Affairs, Vice President of Public Affairs and Manager of Public Affairs have had 5% of their salaries designated as potentially related to lobbying activities to comply with the strictest application of the term and that amount is excluded from the rate in this case.[92] Atmos Energy believes it has complied with the Commission's directive in Case 2018-00281, all relevant legal requirements of lobbying activities and consequently, no additional adjustment is necessary to account for lobbying expenses.

G. The Portion of American Gas Association ("AGA") Dues Included in this Case Are Appropriate for Inclusion in Rates.

Atmos Energy excluded identifiable portions of American Gas Association ("AGA") and Kentucky Chamber of Commerce ("KCC") from rates. For excluding a portion of AGA dues relating to lobbying activities, Atmos Energy looked at 2020 and 2021 AGA dues invoices. The 2020 invoice indicates that 6.2% of AGA dues are allocable to lobbying whereas the 2021 invoice indicates that 3.8% of AGA dues are allocable to lobbying. To be conservative, Atmos Energy elected to use the 2020 percentage and excludes 6.2% of AGA dues from the forecasted test year revenue requirement.

For excluding a portion of Kentucky Chamber of Commerce dues relating to lobbying

[91] Christian Direct Testimony at 43.
[92] *See* Taylor Direct Testimony at 27; Atmos Energy's Response to Staff's Third Request, Item 13.

activities, Atmos Energy looked at Kentucky Chamber of Commerce dues invoices. Kentucky Chamber of Commerce invoices that indicate 85% of dues are not allocable to lobbying activity -- thus 15% of dues are allocable to lobbying. Therefore, Atmos Energy has excluded 15% of Chamber of Commerce dues from the forecasted test year revenue requirement. The dues amounts for AGA and the Chamber of Commerce that Atmos Energy excludes from the forecasted test year revenue requirement are included in attachments to discovery responses.[93]

H. Late Payment Fees and Miscellaneous Service Revenues

Atmos Energy has provided several analyses and responses throughout the discovery process regarding late payment fess and supporting miscellaneous services revenues. Late payment charge is authorized under 807 KAR 5:006, Section 9(3)(h). This fee is included in a utility's tariff to encourage the customer to pay promptly. Late payments fees currently comprise approximately $1.4 million in revenues in the Company's filing, and if the late payments fees were to be removed from the tariff this adjustment would need to be reallocated to base rates in the Company's filing.[94] The impact on payment lag would be negative but an adjustment cannot be calculated with certainty until the next case.

The Commission has asked Atmos Energy about late payment fees in scenarios involving low-income assistance programs. Atmos Energy is willing to consider changing its policy for these scenarios and has suggested the best way is outside the context of this rate case filing to work in conjunction with the Commission and how it would be best applied with the low-income assistance options available and reflect any changes in the Company's next case.[95] Atmos Energy also is amenable to a more comprehensive approach would consider changing its policy to eliminate late fees from its tariff altogether, and to recover the revenue through base rates.[96] The Company would also

[93] Atmos Energy's Response to OAG's First Request, Item 2.
[94] Atmos Energy's Response to Staff's Third Request, Item 11; *see also* Densman Direct Testimony, Exhibit JDH-5.
[95] Atmos Energy's Response to Staff's Sixth Request, Item 3.
[96] *Id*.

consider this same approach for miscellaneous service fees as well.[97] For this alternative approach, the Company would recommend the policy be applied within this rate case in order to reallocate revenues to base rates. For miscellaneous services revenues to be eliminated, and the resulting revenue that would shift to base rates is approximately $234,286.[98]

III. CONCLUSION

The three most significant elements of this rate case are capital structure, return on equity and the revision to the PRP tariff. These three issues have the greatest impact on the revenue generated by rates. These are also the most contested issues by the OAG. The evidence presented by Atmos Energy meets the test of substantial and credible. In contrast, the OAG's testimony is generally unsupported, inconsistent with prior case testimony and focused solely on minimizing rates, rather than developing reasonable rates based on the record.

The Commission has over the last few years has recognized the need for structured, long-term pipeline replacement mechanisms for certain pipe materials to address a subset of the aging infrastructure of the gas industry as well as the growing concern for the safe, reliable operation of those systems. As this case demonstrates, Atmos Energy is attempting to proactively replace its system by targeting high-risk areas and having a long-term replacement plan based on risk while balancing the financial impact to customers. In addition, Atmos Energy is attempting to ensure its systems have adequate capacity to allow for residential and industrial growth to occur, as a growing system helps both economic development as well as potentially lowering costs for existing customers. However, the physical and financial limitations imposed on that effort in the prior two rate cases have placed the Company in a difficult position. A Commission limit on non-bare steel expenditures, combined with a limit on bare steel expenditures, forces Atmos Energy to be unable to proactively target a significant portion of prudent, currently needed replacements of undisputedly unsafe pipe, including Aldyl-A, as well as

[97] *Id.*
[98] Densman Direct Testimony, Exhibit JDH-5.

limit economic development and growth opportunities in the Commonwealth.

To ensure continued safety and reliability of its system, the Company is proposing the inclusion of incremental investment in the Company's existing PRP tariff to begin targeting the long-term replacement of Aldyl-A. The Company has provided a detailed scope for its proposed Aldyl-A projects for Fiscal Year 2022 and Fiscal Year 2023 in this Case as part of its long-term approach to replacing Aldyl-A based on risk. The Company will continue to file these project-level details for the Commission's approval of part of its annual PRP filings should Aldyl-A be included within the PRP tariff. The need and prudency of the projects is unchallenged. The testimony of the Company's witnesses describes the condition of the portions of the system to be replaced, the standards for determining replacement and the applicable state and national safety standards applicable to Atmos Energy. The only objection from the Attorney General is one of timing, not prudency. Yet, he has not provided any evidence to support his demand for deferral of unquestioned safety upgrades to protect the public – his clients. His only objection is to keep rates lower than proposed.

Simultaneously, the Commission's limitation on the Company's non-PRP capital spending is detrimental to the Company, its customers, and the Commonwealth of Kentucky. The non-PRP limitation has a chilling effect on encouraging economic development, and significantly constrains the Company more and more each year as the limit is a fixed amount, and as prices are increasing across the country. All non-PRP capital is subject to Commission review for prudency in the Company's rate case and the Commission still maintains complete discretion in analyzing the Company's capital spending. The non-PRP spending limitation to a fixed amount presents a mounting risk to the Company's ability to operate a safe and reliable system as it severely hinders the Company's flexibility to address the needs of its system, as well as take advantage of economic development opportunities which they materialize.

The Commission should continue its current policy of encouraging replacement of aging, leaking, unreliable pipelines. The Company's proposal sets out a well-defined, fiscally responsible program to address the safety of its system. Each of those situations is distinguishable based on needs, operational factors, regulatory mandates and project specific requirements.

The issue is whether based on the evidence in this record, Atmos Energy has demonstrated that its replacement proposal, its budgeting reliability and its efforts to maintain a safe pipeline system in Kentucky is reasonable. Failing to actively address the known safety issues now will only increase the cost and customer rates in the future and may jeopardize public safety to an unnecessary degree. The practice of delaying expenditures to future ratepayers has unfortunately occurred for many years in other scenarios in Kentucky, such as public infrastructure like roads and bridges. The Commission is urged to reject the Attorney General's recommendation to defer needed pipe replacement, and allow, indeed encourage, the Company's need to invest capital into the Commonwealth to enhance the safety and reliability of its system. Modest rate adjustments in alignment with responsible infrastructure replacement is a much more justifiable regulatory policy than continually deferring rate increases and safety projects to the next case as the Attorney General demands. That deferral creates a never-ending cycle resulting in situations needing extensive immediate system reconstruction and the associated spike in rates and surcharges, such as those the Commission is facing with many of its water systems. Prudent management of current system needs is preferable to crisis management of foreseeable but unaddressed incidents in the future.

Essential to meeting the ongoing safety and operational needs f the Company is the allowance of a reasonable ROE. Given the contrast in the level of detail, analysis, and supporting evidence filed by the respective witnesses of the parties, the Company has more than met its burden of justifying the proposed ROE. In contrast to recent cases involving other gas LDCs' that settled for a ROE based on a number of non-market factors, Atmos Energy has chosen to base its ROE on actual

market conditions as reflected in the undisputed analysis of its expert witness. Given the current market conditions and the failure of the OAG to provide any credible substantive evidence to the contrary, the proposed ROE should be allowed.

Atmos Energy requests that its proposed rates, inclusion of Aldyl-A within its PRP tariff, removal of capital expenditures limitations, and safety replacement proposals be approved.

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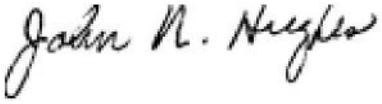

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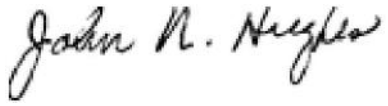
CERTIFICATE

In accordance with the requirements of 807 KAR 5:001(8), I certify that this electronic filing is true and accurate; that the electronic filing has been transmitted to the Commission on January 14, 2022; and that no party has been excused from participation by electronic means.



ATMOS ENERGY CORPORATION - KENTUCKY
SUMMARY OF REVENUE AT PRESENT AND PROPOSED RATES
TEST YEAR ENDING DECEMBER 31, 2022

Line No.	Description	Block (Mcf)	Test Year Ending 12/31/2022 Number of Bills, Units	Volumes	Current Rate	Current Revenue	Proposed Rate	Proposed Revenue
			(a)	(b)	(c)	(d)	(e)	(f)
1	Residential Sales							
2	Firm Sales (G-1)	Customer Chrg	1,930,462		$20.68	$39,921,954	$24.00	$46,331,088
3		0 - 300		10,018,608	1.3855	13,880,782	1.6205	16,235,155
4		301 - 15,000		0	0.9578	0	1.1260	0
5		Over 15,000		0	0.7651	0	0.9300	0
6		Gas Costs				46,393,776		46,393,776
7	Total		1,930,462	10,018,608		100,196,512		108,960,019
8	Increase Amount							8,763,507
9	Increase Percentage							8.7%
10								
11	Commercial Sales							
12	Firm Sales (G-1)	Customer Chrg	218,719		$56.25	$12,302,944	$66.00	$14,435,454
13		0 - 300		4,410,839	1.3855	6,111,218	1.6205	7,147,765
14		301 - 15,000		642,678	0.9578	615,557	1.1260	723,655
15		Over 15,000		0	0.7651	0	0.9300	0
16	Interruptible Sales (G-2)	Customer Chrg	34		$455.56	15,489	$520.00	17,680
17		0-15,000		13,251	0.8566	11,351	1.0000	13,251
18		Over 15,000		1	0.6570	1	0.8200	1
19		Gas Costs				23,466,989		23,466,989
20	Total		218,753	5,066,769		42,523,549		45,804,795
21	Increase Amount							3,281,246
22	Increase Percentage							7.7%
23								
24	Industrial Sales							
25	Firm Sales (G-1)	Customer Chrg	2,607		56.25	$146,644	66.00	$172,062
26		0 - 300		283,794	1.3855	393,196	1.6205	459,887
27		301 - 15,000		357,703	0.9578	342,608	1.1260	402,774
28		Over 15,000		0	0.7651	0	0.9300	0
29	Interruptible Sales (G-2)	Customer Chrg	63		455.56	28,700	520.00	32,760
30		0-15,000		203,548	0.8566	174,359	1.0000	203,548
31		Over 15,000		49,469	0.6570	32,501	0.8200	40,564
32		Gas Costs				3,823,518		3,823,518
33	Total		2,670	894,513		4,941,526		5,135,113
34	Increase Amount							193,587
35	Increase Percentage							3.9%
36								
37	Public Authority Sales							
38	Firm Sales (G-1)	Customer Chrg	18,401		56.25	$1,035,056	66.00	$1,214,466
39		0 - 300		761,797	1.3855	1,055,470	1.6205	1,234,492
40		301 - 15,000		141,842	0.9578	135,856	1.1260	159,714
41		Over 15,000		0	0.7651	0	0.9300	0
42		Gas Costs				4,186,470		4,186,470
43	Total		18,401	903,639		6,412,852		6,795,142
44	Increase Amount							382,290
45	Increase Percentage							6.0%

ATMOS ENERGY CORPORATION - KENTUCKY
SUMMARY OF REVENUE AT PRESENT AND PROPOSED RATES
TEST YEAR ENDING DECEMBER 31, 2022

Line No.	Description	Block (Mcf)	Test Year Ending 12/31/2022 Number of Bills, Units	Volumes	Current Rate	Current Revenue	Proposed Rate	Proposed Revenue
			(a)	(b)	(c)	(d)	(e)	(f)
1	Transportation							
2	Customer Charges (T-4)	Customer Chrg	1,429		458.20	654,589	520.00	742,877
3	Customer Charges (T-3)	Customer Chrg	838		457.97	383,779	520.00	435,760
4	Customer Charge (SpK)	Customer Chrg	151		435.00	65,820	435.00	65,820
5	Transp. Adm. Fee	Customer Chrg	2,387		50.00	119,350	50.00	119,350
6	Parked Volumes [1]			1,181,697	0.10	118,170	0.00	0
7	EFM Charges					135,825		135,825
8	Firm Transportation (T-4)	0 - 300		412,985	1.4508	599,159	1.6205	669,243
9		301 - 15,000		5,249,162	1.0030	5,264,909	1.1260	5,910,556
10		Over 15,000		1,712,468	0.8012	1,372,029	0.9300	1,592,595
11	Economic Dev Rider (EDR)	301 - 15,000		0	0.7184	0	0.8445	0
12		Over 15,000		23,465	0.5738	13,465	0.6975	16,367
13	Interruptible Transportation (T-3)	0 - 15,000		4,937,981	0.8760	4,325,671	1.0000	4,937,981
14		Over 15,000		3,405,818	0.6719	2,288,369	0.8200	2,792,771
15	Total Special Contracts			15,125,542	Various	2,516,787	Various	2,516,787
16		Gas Costs				0		0
17	Total		2,418	30,867,422		17,857,922		19,935,932
18	Increase Amount							2,078,010
19	Increase Percentage							11.6%
20								
21	Service Charges/Late Payment Fees							
22	Total					1,534,566		1,642,646
23	Increase Amount							108,080
24	Increase Percentage							7.0%
25								
26	TOTAL							
27	Total		2,172,704	47,750,951		173,466,927		188,273,647
28	Increase Amount							14,806,720
29	Increase Percentage							8.5%
30								
31	[1] Parked Volumes not included in Total Deliveries.							

ATMOS ENERGY CORPORATION - KENTUCKY
SUMMARY OF REVENUE AT PRESENT AND PROPOSED RATES
TEST YEAR ENDING DECEMBER 31, 2022

Line No.	Description	Block (Mcf)	Test Year Ending 12/31/2022 Number of Bills, Units	Volumes	Current Rate	Current Revenue	Proposed Rate	Proposed Revenue
			(a)	(b)	(c)	(d)	(e)	(f)
1	Sales							
2	Firm Sales (G-1)	Customer Chrg	1,930,462		$20.68	$39,921,954	$24.00	$46,331,088
3		Customer Chrg	239,727		56.25	13,484,644	66.00	15,821,982
4		0 - 300		15,475,038	1.3855	21,440,666	1.6205	25,077,299
5		301 - 15,000		1,142,223	0.9578	1,094,021	1.1260	1,286,143
6		Over 15,000		0	0.7651	0	0.9300	0
7	Interruptible Sales (G-2)	Customer Chrg	97		455.56	44,189	520.00	50,440
8		0 - 15,000		216,799	0.8566	185,710	1.0000	216,799
9		Over 15,000		49,469	0.6570	32,501	0.8200	40,565
10								
11	Transportation							
12	Customer Charges (T4)	Customer Chrg	1,429		458.20	654,589	520.00	742,877
13	Customer Charges (T3)	Customer Chrg	838		457.97	383,779	520.00	435,760
14	Customer Charge (SpK)	Customer Chrg	151		435.00	65,820	435.00	65,820
15	Transp. Adm. Fee	Customer Chrg	2,387		50.00	119,350	50.00	119,350
16	Parked Volumes [1]			1,181,697	0.10	118,170	0.00	0
17	EFM Charges					135,825		135,825
18	Firm Transportation (T-4)	0 - 300		412,985	1.4508	599,159	1.6205	669,243
19		301 - 15,000		5,249,162	1.0030	5,264,909	1.1260	5,910,556
20		Over 15,000		1,712,468	0.8012	1,372,029	0.9300	1,592,595
21	Economic Dev Rider (EDR)	301 - 15,000		0	0.7184	0	0.8445	0
22		Over 15,000		23,465	0.5738	13,465	0.6975	16,367
23	Interruptible Transportation (T-3)	0 - 15,000		4,937,981	0.8760	4,325,671	1.0000	4,937,981
24		Over 15,000		3,405,818	0.6719	2,288,369	0.8200	2,792,771
25	Total Special Contracts			15,125,542	Various	2,516,787	Various	2,516,787
26	Total Tariff		2,172,704	47,750,951		94,061,607		108,760,248
27								
28								
29	Other Revenues					234,286		234,286
30	Late Payment Fees					1,300,280		1,408,360
31	Total Gross Profit					95,596,173		110,402,894
32								
33	Gas Costs					77,870,753		77,870,753
34								
35	Total Revenue					$ 173,466,926		$ 188,273,647
36								
37	Total Adjustment							$14,806,721
38								
39								
40	[1] Parked Volumes not included in Total Deliveries.							