COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF ATMOS ENERGY CORPORATION FOR AN ADJUSTMENT OF RATES	)))	CASE NO. 2021-00214

<u>O R D E R</u>

Atmos Energy Corporation (Atmos Energy) is a utility that delivers natural gas to approximately three million ratepayers in eight states. Atmos Energy has six gas utility operating divisions located in Denver, Colorado (Colorado/Kansas Division); Baton Rouge, Louisiana (Louisiana Division); Flowood, Mississippi (Mississippi Division); Lubbock, Texas (West Texas Division); Dallas, Texas (Mid-Tex Division); and Franklin, Tennessee (Kentucky/Mid-States Division). Atmos Energy's corporate offices are in Dallas, Texas and provide services to its operating divisions such as accounting, legal, human resources, rate administration, procurement, information technology, and customer service organizations. Atmos Energy also has two customer contact centers located in Amarillo and Waco, Texas. The costs of these centralized services are shared with the other Atmos Energy operating divisions, including the Kentucky/Mid-States division. Atmos Energy's regulated gas distribution operation in Kentucky (Atmos Kentucky) serves approximately 179,900 residential, commercial, and industrial customers in central and western Kentucky, with 159,800 of those being residential class customers.[1] Atmos Kentucky last filed for an adjustment of its gas rates in Case No. 2018-00281, which had a final order issued on May 8, 2019.[2]

BACKGROUND

Atmos Kentucky filed an application for an adjustment of rates on June 30, 2021. The application requested an overall rate increase of 9.4 percent or approximately $16.390 million in annual revenue and an increase of 9.6 percent for the average residential customer. Following discovery, the requested increase was reduced to $15.131 million or an 8.8 percent increase on rebuttal. Atmos Kentucky's application was initially rejected due to a filing deficiency, which was cured on July 20, 2021. Pursuant to an Order issued on July 23, 2020, the Commission found that an investigation would be necessary to determine the reasonableness of Atmos Kentucky's proposed rates and suspended the proposed rates for a period of six months, from August 19, 2021, up to and including February 18, 2021, pursuant to KRS 278.190(2). The Attorney General of the Commonwealth of Kentucky, by and through the Office of Rate Intervention (Attorney General) is an intervenor in this proceeding. Pursuant to a procedural schedule established on July 23, 2021 and amended July 30, 2021, Atmos Kentucky filed direct and rebuttal testimony, and responded to multiple rounds of discovery. The Attorney General filed direct testimony and responded to one round of discovery. A three-day hearing was scheduled for December 14-16, 2021. The hearing was canceled due to an emergency created by tornados in the utility's service territory. The parties submitted

[1] Application at 3.

[2] Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment in Rates* (Ky. PSC June 12, 2019).

briefs to the Commission for consideration on January 14, 2022. This mater now stands submitted for a decision based upon the written record.

LEGAL STANDARD

The Commission's statutory obligation when reviewing a rate application is to determine whether the proposed rates are "fair, just and reasonable."[3] Applying that standard, the Commission has held that cost-based rates for investor-owned utilities should be set at a level to allow the utility to recover its reasonable expenses and provide its shareholders an opportunity to earn a fair return on invested capital.[4] However, when a utility proposes a rate increase, "the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the utility."[5] The Commission must review the record in its entirety and apply its expertise to make an independent decision as to the level of rates that should be approved, including terms and conditions of service.

TEST PERIOD

Atmos Kentucky proposed the 12 months ending December 31, 2022, as its forecasted test period to determine the reasonableness of its proposed rates.[6] The

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[3] *See Kentucky Pub. Serv. Comm'n v. Com. ex rel. Conway*, 324 S.W.3d 373, 377 (Ky.2010) ("Because utilities are allowed to charge consumers only 'fair, just, and reasonable rates' under KRS 278.030(1), the [Commission] must ensure that utility rates are fair, just, and reasonable to discharge its duty under KRS 278.040 to ensure that utilities comply with state law.").

[4] Case No. 2017-00481, *An Investigation of the Impact of the Tax Cuts and Job Act on the Rates of Atmos Energy Corporation, Delta Natural Gas Company, Inc., Columbia Gas of Kentucky, Inc., Kentucky-American Water Company, and Water Service Corporation of Kentucky* (Ky. PSC Dec. 27, 2017), Order at 1-2; *see also Com. ex. rel. Stephens v. South Central Bell Tel. Co.*, 545 S.W.2d 927, 931 (Ky. 1976) ("Rates are non-confiscatory, just and reasonable so long as they enable the utility to operate successfully, to maintain its financial integrity, to attract capital and to compensate its investors for the risks assumed.").

[5] KRS 278.190(3); *see also* KRS 278.2209 ("In any formal commission proceeding in which cost allocation is at issue, a utility shall provide sufficient information to document that its cost allocation procedures and affiliate transaction pricing are consistent with the provisions of this chapter.").

[6] Application at 4.

Attorney General did not object to the proposed test period or suggest an alternative test period; it did, however, criticize Atmos Kentucky's development of certain items contained in the proposed test period, as discussed herein. The Commission finds Atmos Kentucky's forecasted test period to be reasonable and consistent with the provisions of KRS 278.192 and 807 KAR5:001, Section 16(6), (7), and (8). Therefore, the Commission accepts the forecasted test period proposed by Atmos Kentucky for use in this proceeding.

VALUATION

Rate Base

Atmos Kentucky proposed a net investment rate base for its forecasted test period of $596.130 million, based on the 13-month average for that period.[7] In response to errors identified in discovery, Atmos Kentucky revised this amount to $583.089 million.[8] In its rebuttal testimony, Atmos Kentucky further revised its proposed rate base to $581.184 million.[9]

The Attorney General proposed to reduce Atmos Kentucky's rate base to $563.372 million.[10] The Attorney General proposed to (1) remove asset net operating loss (NOL) accumulated deferred income taxes (ADIT) due to Winter Storm Uri;[11] (2) reduce asset

[7] Application, Schedule A.

[8] Atmos Kentucky's Supplemental Response to Commission Staff's First Request for Information (filed Aug. 23, 2021), (Staff's First Request), Item 55.

[9] Corrected Rebuttal Testimony of Joe T. Christian (Christian Rebuttal Testimony), Exhibit JTC-R-1 Revised.

[10] Attorney General's Post-Hearing Brief (filed Jan. 14, 2022) (Attorney General's Brief), Atmos_Rev_Req_-_AG_Recommendation-Addtl_Brief_Quantifications.xlsx, Tab Rate Base.

[11] Attorney General's Brief at 5.

NOL ADIT to reflect taxable income from April 2021 through December 2021;[12] (3) include Shared Service Unit (SSU) Division 002 T-Lock Adjustment - Unrealized Gains liability ADIT;[13] (4) remove other SSU division 002 ADIT;[14] (4) remove Accounts Payable – Construction;[15] (5) remove regulatory assets for rate case expenses;[16] (6) adjust depreciation expense lag days in cash working capital (CWC) and remove noncash items;[17] (7) adjust CWC to reflect changes in expenses;[18] and (8) reflect effects from amortization of unprotected excess deferred income taxes (EDIT) over three years.[19]

As discussed later in this Order, the Commission has determined that Atmos Kentucky's net investment rate base for ratemaking purposes is $568.506 million, as shown below.

	Amount
Rate Base per Application	$ 596,130,007
August 23, 2021 Supplemental Filing - Revisions	$ (13,040,183)
Revised Rate Base	$ 583,089,824
Adjustments:	
Include SSU Division 002 T-Lock Adjustment-Unrealized Gains Liability ADIT	$ (3,229,413)
Remove Other SSU Division 002 ADIT	$ (1,218,640)
Remove Accounts Payable - Construction	$ (5,174,457)
Remove Regulatory Asset for Rate Case Expenses	$ (365,168)
Remove Noncash Items from CWC	$ (6,314,237)
Reflect Effects from Amortization of Unprotected EDIT Over Three Years	$ 1,717,920
Net Change in Rate Base	$ (14,583,995)
Adjusted Rate Base	$ 568,505,829

[12] Attorney General's Brief at 6.

[13] Attorney General's Brief at 12.

[14] Attorney General's Brief at 12.

[15] Attorney General's Brief at 13.

[16] Attorney General's Brief at 14.

[17] Attorney General's Brief at 19.

[18] Attorney General's Brief at 19.

[19] Attorney General's Brief at 21.

Capitalization

Atmos Energy conducts utility operations in eight states through unincorporated operating divisions, which are not separate legal entities. All debt or equity funding of each division is issued by Atmos Energy.[20] Atmos Kentucky stated that this consolidated capital structure is appropriate for ratemaking in Kentucky because Atmos Energy provides the debt and equity capital that supports the assets serving Kentucky customers.[21] Atmos Kentucky proposed to update its total capitalization for the forecasted test period to $13,499,336,801 to reflect finance activity and the impact of interest rate swaps.[22] The Attorney General recommended adjustments to the proposed capitalization, as discussed below. The Commission accepts Atmos Kentucky's proposed capitalization amount for ratemaking but, as discussed below, modifies the inherent capital structure.

REVENUE REQUIREMENT ADJUSTMENTS

Atmos Kentucky developed an operating statement for its forecasted test period based on its budgets for the 2022 and 2023 fiscal years, excluding the Pipeline Replacement Program (PRP) expenditure after September 30, 2022.[23] As required by 807 KAR 5:001, Section 16(6)(a), the financial data for the forecasted test period was presented by Atmos Kentucky in the form of pro forma adjustments to its base period, with the 12 months ending September 30, 2021.[24] Based on the assumptions built into

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[20] Direct Testimony of Joe T. Christian (Christian Testimony) at 52.

[21] Christian Testimony at 52-53.

[22] Christian Rebuttal Testimony, Exhibit JTC-R-1.

[23] Christian Testimony at 13. Atmos Kentucky's fiscal year ends September 30.

[24] Application at 4.

its budgets, Atmos Kentucky calculated its test year revenues and operating and maintenance (O&M) expenses to be $173.467 million and $144.049 million, respectively.[25] Based on these adjusted revenues and O&M expenses, Atmos Kentucky's test period operating income was $29.418 million, which based on its proposed rate base, results in a 4.93 percent overall rate of return.[26] Based on a proposed ROE of 10.35 percent, Atmos Kentucky determined that it required a revenue increase of $6.527 million, which includes the amortization of regulatory liabilities of $9.862 million and would produce an overall return on rate base of 7.66 percent.[27]

The Attorney General, based on a number of proposed adjustments to Atmos Kentucky's test period results and a 9.10 percent ROE, recommended an increase in revenues of $0, with a maximum increase of $1.540 million after regulatory liabilities are exhausted.[28]

The Commission will accept components of Atmos Kentucky's test period and certain proposed adjustments but will also accept some of the Attorney General's proposed adjustments. A discussion of the individual adjustments accepted, modified, or rejected by the Commission, and the impact of those adjustments on Atmos Kentucky's revenue requirement follows.

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[25] Application, Schedule C-1.

[26] Application, Schedule A and Schedule C-1.

[27] Application, Schedule A.

[28] Attorney General’s Brief at 38.

Rate Base Adjustments

Remove Asset NOL ADIT due to Winter Storm Uri

Atmos Energy tracks its NOL ADIT, which is a deferred tax asset that increases rate base, on a consolidated company basis for Atmos Energy's utility divisions. Atmos Energy records that deferred tax asset in Division 2, Account 190 and then allocates a share of that NOL ADIT to its Kentucky operations using a cost allocation percentage.[29] A large portion of the NOL ADIT in the base period and forecasted period as originally filed is directly tied to costs from other states arising from Winter Storm Uri. The Attorney General's witness, Lane Kollen, proposed to remove that NOL ADIT before the total was allocated to Kentucky using the allocation percentage,[30] and Atmos Kentucky agreed to the adjustment.[31] The Commission finds that this adjustment is reasonable and is accepted.

Reduction of NOL ADIT from April 2021 through December 2021:

Atmos Energy maintains separate accounting records for each temporary difference and the related deferred tax asset and liability amounts except for deferred tax assets arising from net operating loss carryforwards, or NOL ADIT.[32] Atmos Energy aggregates the NOLs for all divisions and records NOL ADIT at the corporate level in the

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[29] Direct Testimony of Lane Kollen (Kollen Testimony) at 7-8.

[30] Kollen Testimony at 9.

[31] Christian Rebuttal Testimony at 4.

[32] Atmos Kentucky's Response to the Attorney General's First Request for Information (filed Aug. 23, 2022) (Attorney General's First Request), Item 20(a).

SSU Division 002.[33] At the corporate level, Atmos Energy generally only divides NOL ADIT between those that arose from regulated and unregulated operations.[34]

In its revenue model filed with the application, Atmos Kentucky reflected approximately $608.54 million in regulated, or utility, NOL ADIT as of September 30, 2020; $598.05 million in utility NOL ADIT as of December 31, 2021, and $977.07 million in utility NOL ADIT as of March 31, 2021.[35] Upon questioning from the Attorney General, Atmos Kentucky acknowledged that the significant increase in its NOL ADIT balance at the end of March 2021 arose from expenses incurred by rate divisions in Texas, Oklahoma, and Kansas arising from Winter Storm Uri. As noted above, Atmos Kentucky acknowledged NOL ADIT arising from Winter Strom Uri should not be included in rate base for Kentucky customers and, therefore, updated its revenue model to remove those items,[36] which resulted in the utility NOL ADIT being reduced to $537.24 million as of March 31, 2021.[37]

Atmos Kentucky did not reflect any change in its utility NOL ADIT after March 31, 2021. Rather, Atmos Kentucky simply carried the $537.24 million balance forward to the forecasted test year and then allocated it to Kentucky operations using the same sharing

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[33] Kollen Testimony at 7.

[34] *See* Atmos Kentucky's Response to Staff's First Request, Item 55, ADIT_for_KY_04-30-21.xlsx, Tab ADIT 002, Rows 58-60.

[35] *See* Atmos Kentucky's Response to Staff's First Request, Item 55, ADIT_for_KY_04-30-21.xlsx, Tab ADIT 002, Row 59.

[36] Atmos Kentucky's Response to the Attorney General's First Request, Item 20(e)-(g).

[37] *See* Atmos Kentucky's Supplemental Response to Staff's First Request (filed Aug. 17, 2021), Item 55, ADIT_for_KY_04-30-21 updated NOL for URI 8-17-21.xlsx, Tab ADIT 002, Row 59.

percentage it uses to allocate SSU's plant and other rate base items,[38] which resulted in $26.72 million of Atmos Energy's utility NOL ADIT being included in rate base for Kentucky operations.[39] Atmos Kentucky then projected the change in the NOL ADIT allocated to Kentucky during the forecasted test year by comparing the projected tax expense during the test year to the ADIT generated to determine whether the NOL ADIT allocated to Kentucky could be utilized to offset tax expense during the test year, which resulted in a $2.986 million reduction in the NOL ADIT allocated to Kentucky.[40]

Kollen noted that the manner in which Atmos calculates the utilization of its NOL ADIT failed to account for potential changes from April 2021 to December 2021.[41] Kollen stated that Atmos Energy had taxable income on its consolidated return in 2020 and, excluding the expenses associated with Winter Storm Uri, in the first part of 2021. Kollen argued that it was unreasonable for Atmos Kentucky to reflect no change in the NOL ADIT in the period from April 2021 to December 2021.[42] Kollen proposed using Atmos Kentucky's utilization of NOL ADIT from October 1, 2020 through March 31, 2021, which was approximately $71.120 million, to project the utilization of the NOL ADIT during the period from April 1, 2021 through December 31, 2021, which would reduce the NOL ADIT

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[38] *See* Atmos Kentucky's Response to Staff's First Request, Item 55, 2021 KY Rev Req Model.xlsx, Tab B.5 F (showing the allocation of Account 190 for Division 002, which included the regulated NOL Assets).

[39] $537,424,569 x 4.97% = $26,717,590.

[40] *See* Atmos Kentucky's Supplemental Response to Staff's First Request (filed Aug. 17, 2021), Item 55, 2021 KY Rev Req Model – Revised 8-17-21.xlsx, Tab ADIT 002, Row 59; *see also* Kollen Testimony at 10 (discussing how Atmos Kentucky calculated the utilization of NOL Assets).

[41] Kollen Testimony at 10.

[42] Kollen Testimony at 11.

by about $106.679 million.[43] Kollen indicated that this would result in a $0.514 million reduction in the revenue requirement.[44]

Atmos Kentucky argued that Kollen's assumption that it would have $106.679 million in tax expense from April 1, 2021, to December 31, 2021, is not reasonable and, therefore, his proposed adjustment is not reasonable. Atmos Kentucky asserted that during the period from April 1, 2021, to September 30, 2021, which represents the end of Atmos Kentucky's most recent fiscal year, the NOL ADIT increased by $34.9 million. Atmos Kentucky argued that with that increase in the NOL ADIT that the net change in the NOL ADIT in the fiscal year ending September 30, 2021, was a decrease of $36.3 million as opposed to the decrease of about $71.120 million reflected in the revenue model. Thus, Atmos Kentucky urged the Commission to reject Kollen's proposed adjustment.[45]

The Commission agrees that the evidence does not currently support reducing the NOL ADIT during the period from April 1, 2021, to December 31, 2021, as proposed by Kollen. While Atmos Kentucky recorded a reduction in its NOL ADIT in fiscal year 2020, the actual reduction in that year was less than the reduction Atmos Kentucky projected in fiscal year 2021, even assuming no change after March 31, 2021. The actual reduction was also significantly lower than Kollen's projection for fiscal year 2021.[46] Atmos Kentucky's testimony regarding the changes in the NOL ADIT from April 1, 2021 to

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[43] Kollen Testimony at 12.

[44] Kollen Testimony at 13.

[45] Rebuttal Testimony of Joey J. Multer (Multer Testimony) at 7-10.

[46] *See* Atmos Kentucky's Response to the Attorney General's First Request, Item 15, AG_1-15_Att1 – NOL Rollforward (CONFIDENTIAL).xlsx.

September 30, 2021 is also credible given that the retail sales of gas distribution companies tend to peak in the winter.[47] Finally, although Atmos Kentucky did not project the utilization of NOL ADIT from October 1, 2021 to December 31, 2021 in either its direct or rebuttal testimony, utilization during that period would not likely exceed the increase in NOL ADIT reflected by Atmos Kentucky from April 1, 2021 to September 30, 2021.[48] Thus, the Commission does not accept Kollen's proposed adjustment to reflect the utilization of additional NOL ADIT during the period from April 1, 2021 to December 31, 2021.

The Commission does question Atmos Kentucky's methodology for tracking and allocating net operating losses. The accumulation and utilization of NOLs should be done on a Kentucky specific basis to the extent possible.[49] Atmos Kentucky has acknowledged that "specific one-off events" resulting in deferred tax liabilities and corresponding NOL ADIT should be assigned to the applicable utility division to the extent they can be identified and the assignment would not violate the consistency rule.[50] Atmos Kentucky even separately tracks and excludes the utilization of NOL ADIT by its non-regulated

[47] The historical portion of the forecasted period reflects this variability in utilization of utility NOL Assets with $10,498,762 being utilized from October 1, 2020, to December 31, 2020, and $60,620,743 being utilized from January 1, 2021, through March 31, 2021. *See* Atmos Kentucky's Supplemental Response to Staff's First Request (filed Aug. 17, 2021), Item 55, ADIT_for_KY_04-30-21 updated NOL for URI 8-17-21.xlsx, Tab ADIT 002, Row 59.

[48] *See* Atmos Kentucky's Supplemental Response to Staff's First Request, Item 55, ADIT_for_KY_04-30-21 updated NOL for URI 8-17-21.xlsx, Tab ADIT 002, Row 59 (reflecting the change in the previous year during the same period).

[49] *See* Case No. 2021-00183, *Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; Issuance of a Certificate of Public Convenience and Necessity; and Other Relief* (Ky. PSC Dec. 28, 2021), final Order at 14-20.

[50] Atmos Kentucky's Response to the Attorney General's First Request, Item 17.

divisions, which results in more NOL ADIT being allocated to utility divisions.[51] However, Atmos Energy apparently makes little to no effort to identify and allocate NOLs to the specific utility division that generated them.[52]

Atmos Energy's failure to track and allocate NOLs to specific utility divisions could result in significant NOL ADIT generated by other jurisdictions being included in rate base for Kentucky customers. Further, it could prevent NOL ADIT properly allocated to Kentucky operations from being utilized by positive taxable income in Kentucky. Those effects would be similar to including ADIT or plant in service from other jurisdictions in rate base for Kentucky, which would be improper.[53]

The Commission recognizes that Atmos Energy has been tracking its NOL ADIT on a consolidated basis and then allocating the NOL ADIT to various divisions for some time and that the method could result in a reasonable allocation if the allocation percentage is appropriate. However, Atmos Kentucky's initial inclusion of $439.64 million arising from losses in other jurisdictions in the NOL ADIT to be allocated raises questions about Atmos Kentucky's method for allocating NOL ADIT to Kentucky customers and the

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[51] *See* Atmos Kentucky's Supplemental Response to Staff's First Request, Item 55, ADIT_for_KY_04-30-21 updated NOL for URI 8-17-21.xlsx, Tab ADIT 002, Row 58 (showing NOL Assets for nonregulated activity of ($170,609,458) as of March 31, 2021, which indicates that the nonregulated divisions utilized significant amounts of net operating losses generated by utility divisions such that the utility NOL Assets actually would not exist in their entirety if NOL Assets actually were determined on a consolidated basis).

[52] Atmos Kentucky does not reflect any federal NOL Assets in the other Kentucky related divisions about which information was provided herein and the only specific item identified for Division 002 is the NOL Asset associated with Winter Strom Uri. *See* Atmos Kentucky's Supplemental Response to Staff's First Request (filed Aug. 17, 2021), Item 55, 2021 KY Rev Req Model – Revised 8-17-21.xlsx. Moreover, Atmos Kentucky did not identify and carve out the NOL Asset associated with Winter Strom URI until the Attorney General asked about it in requests for information, despite the fact that it increased the total NOL Assets by about 82 percent.

[53] *See* Case No. 2021-00183, *Columbia Gas of Kentucky, Inc.* (Ky. PSC Dec. 28, 2021), final Order at 14-20.

reasonableness of using sharing percentages. Thus, in light of the potentially significant losses being incurred by other divisions that might be assigned to Kentucky customers, the Commission finds that Atmos Kentucky's failure to identify and allocate NOLs to specific utility divisions is unreasonable going forward.

Atmos Kentucky must now track the generation and utilization of NOL ADIT for Kentucky in each fiscal year on a standalone basis based on the expenses incurred and revenue generated from regulated operations in Kentucky, including any revenue from Atmos Kentucky's performance-based rates, without regard to losses incurred by other jurisdictions. In future applications to increase base rates, Atmos Kentucky must file a report showing the generation and utilization of NOL ADIT for Kentucky since this Order based on the expenses incurred and revenue generated from Kentucky operations. If Atmos Kentucky proposes to use a different method to reflect the generation and utilization of NOL ADIT for Kentucky in its revenue model in such cases, Atmos Kentucky must explain in detail why using that method would be reasonable.

<u>SSU Division 002 T-Lock Unrealized Gains Liability ADIT</u>

Kollen proposed adjustments to SSU Division 002 ADIT to be consistent with prior rate cases and match asset and liability balance allocations.[54] Atmos Kentucky excluded liability ADIT related to unrealized gains from treasury lock financial hedges (T-Lock) while including the asset ADIT related to realized gains.[55] Kollen argued that this exclusion inappropriately matched allocated ADIT items and differs from the allocations from prior rate cases. Kollen further argued that these amounts together are proper to

[54] Kollen Testimony at 14.

[55] Kollen Testimony at 13-14.

include in Atmos Kentucky's rate base because the amortization of these unrealized and realized gains are used to calculate the average cost of debt.[56] The proposed revenue requirement reduction is $0.313 million.[57]

Atmos Kentucky argued that neither the unrealized gain nor the associated liability ADIT should be included in rate base but agreed that the unrealized gains are included in the common equity used to calculate the weighted average cost of capital (WACC); Atmos Kentucky agreed to Kollen's adjustment as long as there is no reduction to the common equity component.[58]

While the Commission will adjust Atmos Kentucky's capital structure as described below, the adjustment is unrelated to the inclusion of unrealized gains. Atmos Kentucky also did not rebut Kollen's arguments that Atmos Kentucky's methodology is inconsistent with past rate cases and results oriented. Therefore, the Commission finds that this adjustment is reasonable and is accepted.

<u>Other NOL ADIT Adjustments – SSU Division 002</u>

Kollen recommended removing other SSU Division 002 ADIT that was allocated to the Kentucky division because the underlying temporary differences are not allocated to Kentucky. These ADIT amounts include: (1) asset Self-Insurance Adjustment; (2) asset Rabbi Trust, VEBA Trust Contribution Adjustment, and FAS106 Adjustment; (3) Pension Expense; (4) asset Federal and State Tax Interest; (5) asset FD-NOL Credit

[56] Kollen Testimony at 15.

[57] Kollen Testimony at 16.

[58] Rebuttal Testimony of Joel J. Multer (Multer Rebuttal Testimony) at 5-6.

Carryforward – Other; and (6) asset state Enterprise Zone ITC and related Valuation Allowance.[59] The revenue requirement reduction is $0.118 million.

Atmos Kentucky agreed with the various ADIT adjustments related to allocations from SSU Division 002.[60]

The Commission finds that this adjustment is reasonable and is accepted.

Accounts Payable – Construction

Kollen argued that Atmos Kentucky included, in the test period rate base, working capital allowances for gas stored underground and materials/supplies inventories, but failed to subtract any accounts payable liability balance sheet amounts.[61] Kollen stated that the accounts payable amounts represent temporary vendor financing at 0 percent cost to Atmos Kentucky for both operating expenses and capital expenditures.[62] Kollen proposed to subtract it from rate base through the cash working capital (CWC) calculation using the lead/lag approach. The effect is a reduction in the revenue requirement deficiency and requested base increase of $0.501 million.

Atmos Kentucky disagreed with Kollen's recommendation, stating that Atmos Kentucky has followed the same methodologies as was filed and approved in Case Nos. 2017-00349[63] and 2018-00281. Atmos Kentucky argued that Kollen is introducing a new methodology that has not been included in Atmos Kentucky's previous lead/lag studies

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[59] Kollen Testimony at 16-17.

[60] Multer Rebuttal Testimony at 4.

[61] Kollen Testimony at 19.

[62] Kollen Testimony at 20.

[63] Case No. 2017-00349, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates and Tariff Modifications* (Ky. PSC May 3, 2018).

and cherry picks one methodological item in the CWC calculation.[64] Atmos Kentucky also stated that although a similar adjustment was accepted by the Commission in Case No. 2020-00174[65] and in a recent settlement, Kollen provided no support for this adjustment.[66]

In a number of recent base rate cases where the revenue requirement is determined using rate base, the Commission has accepted adjustments to remove accounts payable from working capital amounts because the utility does not finance these amounts. The same reasoning exists here. Therefore, the Commission finds that this adjustment is reasonable and is accepted.

Remove Regulatory Asset for Rate Case Expenses

In the Application, Atmos Kentucky proposed an adjustment to include, in rate base, the 13-month average of the projected unamortized balance of two regulatory assets: (a) deferred rate case expenses in Case No. 2018-0281 of $0.063 million; and (b) projected rate case expenses in the instant case of $0.302 million.[67]

Kollen argued that the deferred rate case expenses were and will be incurred to benefit Atmos Kentucky and its shareholders, not customers, and should be removed.[68] Furthermore, Kollen stated that if Atmos Kentucky's base rates are not reset within the next three years, then it will continue to recover the amortization expense. Kollen

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[64] Christian Rebuttal Testimony at 21-22.

[65] Case No. 2020-00174, *Electronic Application of Kentucky Power Company for (1) A General Adjustment of Its Rates for Electric Service; (2) Approval of Tariffs and Riders; (3) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; (4) Approval of a Certificate of Public Convenience and Necessity; and (5) All Other Required Approvals and Relief* (Ky. PSC June 23, 2020).

[66] Christian Rebuttal Testimony at 22.

[67] Application, Schedule F-6.

[68] Kollen Testimony at 21.

recommended allocating the return on the regulatory asset for the deferred rate case expenses to Atmos Kentucky and its shareholders and allocating the amortization expense to the Atmos Kentucky's customers. The effect is a reduction of $0.023 million in the revenue requirement.

Atmos Kentucky argued that customers benefit from just and reasonable rates, and that it would not recover certain assets, such as capital investments, until after a full rate case, so the inclusion of the regulatory asset in rate base would not provide a material benefit to shareholders to delay rate cases in order to collect amortization expense.[69]

The Commission agrees that rate case expense regulatory assets should not be included in rate base, as that would allow a return on the unamortized balance of the expense. The Commission has historically excluded this item from rate base to share the cost of rate proceedings between the stockholders and ratepayers, notwithstanding omissions of this adjustment in recent Atmos Kentucky rate cases. While Kollen stated that the proposed adjustment removed these regulatory assets from rate base, it removed the $0.241 million increase in the 13-month average rate base from the base period, which included the regulatory asset for Case No. 2018-00281. The Commission will remove the 13-month average of both regulatory assets from rate base of $0.365 million, which results in a revenue requirement reduction of $0.035 million.

Cash Working Capital

Atmos Kentucky included CWC in its rate base of negative $3.063 million based on a lead/lag study that included noncash items.[70] Kollen argued that depreciation

[69] Christian Rebuttal Testimony at 25.

[70] Christian Testimony, 2 Exhibit JTC-4 at 2.

expense should not be included in a lead/lag study with 0 lag days.[71] He recommended that either the expense be removed, or the lag days increased to 27.92 days.[72] Kollen proposed to increase the lag days, which results in a revenue requirement reduction of $0.153 million.[73] Kollen also recommended adjusting the CWC to account for the corrections that Atmos Kentucky filed and for the other adjustments recommended by Kollen and Baudino; the effect is a revenue requirement reduction of $0.093 million.[74] The Attorney General included an additional adjustment to remove noncash items, excluding depreciation; the additional adjustment is a revenue requirement reduction of $0.362 million.[75] In response to data requests, Kollen also provided the adjustment necessary to remove noncash items from the lead/lag study, a rate base reduction of $6.314 million, and a revenue requirement reduction of $0.612 million.[76]

Atmos Kentucky argued that Kollen's adjustment incorrectly describes when depreciation expense is recovered from customers and that it is actually recovered after service is provided.[77] Atmos Kentucky agreed that adjustments to expenses should be flowed through the lead/lag study and provided this correction.[78]

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[71] Kollen Testimony at 24.

[72] Kollen Testimony at 26.

[73] Kollen Testimony at 26.

[74] Kollen Testimony at 27.

[75] Attorney General's Brief at 19.

[76] Attorney General's response to Commission Staff's First Request for Information, Item 2.

[77] Christian Rebuttal Testimony at 24.

[78] Christian Rebuttal Testimony at 24.

Noncash expenses are not appropriate to include in the CWC determination. The Commission finds that noncash items should be removed from the lead/lag study and accepts Kollen's calculated adjustment for a revenue requirement reduction of $0.612 million.

Pipeline Replacement Program

Atmos Kentucky proposed to include capital projects for its PRP in base rates and reset its rider to $0 through September 2022, and, as discussed below, to expand its PRP to include the accelerated replacement of Aldyl-A pipe. Atmos's PRP was last rolled into base rates in Case No. 2018-00281. Kollen recommended that the Commission reject the inclusion of Aldyl-A in the PRP.[79]

As discussed below, the Commission finds that Atmos Kentucky provided sufficient information to justify the Aldyl-A replacement projects included in its forecasted test year and the proposal to include these projects in base rates and roll the PRP into base rates through September 2022 is reasonable and is approved. However, in Atmos Kentucky's next base rate case, the Commission will consider the justness of resetting PRP rates. Rolling PRP amounts in rate base and resetting the PRP rider to $0 reduces the transparency of the amounts expended as part of the rider.

Amortize Unprotected Excess Deferred Income Taxes (EDIT)

Atmos Kentucky proposed a five-year amortization of its unprotected EDIT regulatory liability. Kollen recommended a three-year amortization period to return these amounts between rate cases, consistent with the amortization of rate case expenses.[80]

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[79] Kollen Testimony at 46-47.

[80] Kollen Testimony at 30.

The effect on rate base is an increase of $1.718 million, because the unprotected EDIT regulatory liability is a reduction to rate base and increasing the amortization will decrease the 13-month average balance deducted from rate base.

Atmos Kentucky did not oppose Kollen's adjustment but stated that a longer amortization period benefits customers for a longer period and recommended using the proposed five-year amortization period.[81]

The Commission finds that Kollen's adjustment to amortize unprotected EDIT over three years is reasonable and is accepted. The rate base increase results in a revenue requirement increase of $0.166 million and the increased amortization, which is discussed below, results in a revenue requirement decrease of $3.460 million. In conjunction with the amortization of regulatory liabilities discussed below, decreasing the amortization period for unprotected EDIT will ameliorate the current rate increase to the benefit of customers.

Operating Income Adjustments

Reduce Outside Services Expense Allocated from Kentucky/Mid-States Division

For both the base period and forecasted test period, Atmos Kentucky included $1.489 million in outside services expense allocated from the Kentucky/Mid-States division,[82] which Kollen argued is excessive compared to historical expenses and driven by increases that did not actually occur in the base period updates.[83] Kollen

[81] Christian Rebuttal at 32.

[82] Christian Testimony, Exhibit JTC-2.

[83] Kollen Testimony at 28-29. *See* also Atmos Kentucky's response to the Attorney General's Second Request for Information, Item 11.

recommended annualizing the actual expenses incurred in the base period for a revenue requirement reduction of $0.405 million.[84]

Atmos Kentucky argued that the now available actual results of the base period do not support Kollen's adjustment.[85] Atmos Kentucky argued that selecting a single expense category was not appropriate because while outside services expense was lower than projected, the total operations and maintenance (O&M) expenses are 2.25 percent higher, including bad debt expense and 0.42 percent lower excluding bad debt.[86]

The Commission finds that Kollen's adjustment is reasonable and is accepted. While the total O&M expenses are relatively close to projections, Atmos Kentucky did not forecast its total O&M expenses by simply carrying over the base period amount. The outside services expenses included in the test-year are not reasonable given the historic amounts and Atmos Kentucky's stated drivers of the increase.

Amortization of EDIT

As discussed above, Kollen recommended a 3-year amortization period for Atmos Kentucky's unprotected EDIT. The effect of increasing the amortization of the regulatory liability is a revenue requirement reduction of $3.460 million.

The Commission finds that this adjustment is reasonable and is accepted.

Amortize Remaining Rate Case Expense from Case No. 2018-00281

Atmos Kentucky proposed a three-year amortization of rate case expenses consistent with the Commission's findings and final Order in Case No. 2018-00281,

[84] Kollen Testimony at 29.

[85] Christian Rebuttal at 27.

[86] Christian Rebuttal at 27.

resulting in amortization expense of $0.149 million.[87] Kollen proposed and Atmos Kentucky agreed to reset the amortization for the regulatory asset related to Case No. 2018-00281 so that the amortization runs concurrently with the present case, resulting in amortization expense of $0.138 million. This results in a revenue requirement reduction of $0.011 million.

The Commission finds that this adjustment is reasonable and is accepted.

Remove Social Organization/Service Club Dues

In its application, Atmos Kentucky included $0.052 million for American Gas Association (AGA) dues in the test year, after an adjustment to remove $0.003 million for lobbying activities. Kollen argued that AGA dues are like Edison Electric Institute (EEI) dues, which have been disallowed in previous cases.[88] Further, Kollen suggested that Atmos Kentucky has not provided proof that the dues its ratepayers provide toward Atmos Kentucky's membership in AGA are not used for legislative advocacy, regulatory advocacy, or public relations.[89] Kollen recommended removing all AGA dues in the test year.

Atmos Kentucky explained that 6.2 percent of AGA and 15 percent of Kentucky Chamber of Commerce dues related to legislative advocacy were removed from the forecasted test year revenue requirement, based upon amounts identified on invoices as allocable to lobbying activity.[90] Atmos Kentucky argued that its participation in AGA

[87] Application, Schedule F-6.

[88] Kollen Testimony at 35.

[89] Kollen Testimony at 35.

[90] Atmos Kentucky's response to the Attorney General's First Request for Information (Attorney General's First Request), Item 2.

benefits customers in that it enables them to stay aware of changes and implement best practices to provide safe, reliable, and efficient delivery of natural gas to its customers. Atmos Kentucky also provided an explanation of select organizations for which it included dues in base rates and stated that the remaining organizations are local, and state civic organizations engaged in the overall economic development in and around Atmos Kentucky's service area.[91]

As noted in Case Nos. 2020-00350 and 2021-00183, Atmos Kentucky has the burden of establishing that costs it seeks to recover in rates for dues paid to associations like AGA do not include prohibited costs for lobbying and political activity, including costs for legislative lobbying, regulatory advocacy, and public relations.[92] When asked by the Attorney General whether each association for which dues were included in rates engaged in such activity, Atmos Kentucky indicated that it "identified the AGA and Kentucky Chamber of Commerce as organizations that engage, directly or indirectly, in one or more of the listed activities," without indicating whether or not others did.[93] Atmos Kentucky then estimated percentages of the dues related only to lobbying for the AGA and Kentucky Chamber of Commerce without identifying amounts paid for other

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[91] Atmos Kentucky's response to the Attorney General's First Request for Information, Item 2.

[92] Case No. 2020-00350, *Electronic Application of Louisville Gas and Electric Company for an Adjustment of Its Electric and Gas Rates, a Certificate of Public Convenience and Necessity to Deploy Advanced Metering Infrastructure, Approval of Certain Regulatory and Accounting Treatments, and Establishment of a One-Year Surcredit* (Ky. PSC June 30, 2021), final Order 27-30. Case No. 2021-00185, *Electronic Application of Delta Natural Gas Company, Inc. for an Adjustment of Its Rates and a Certificate of Public Convenience and Necessity* (Ky. PSC Jan. 3, 2022), final Order 9-10.

[93] Atmos Kentucky's Response to the Attorney General's First Request, Item 2(d); *see also* Atmos Kentucky's Response to the Attorney General's First Request, Item 2(c), Attachment 2. The provided description for Girls Inc. included "we also advocate for legislation and policies."

prohibited costs.[94] Thus, the Commission finds that Atmos Kentucky has not met its burden of proof that the association and social organization/social club dues are properly recoverable from ratepayers and do not include expenses related to legislative advocacy, regulatory advocacy, or public relations.[95] The Commission will remove all such dues, excluding the Southern Gas Association, because it has been specifically approved in recent gas rate cases.[96] The Commission will also exclude expenses included in error.[97] The resulting revenue requirement reduction is $0.164 million.

Uncollectible Accounts

Atmos Kentucky proposed to establish a regulatory asset that would defer write-offs until the next base rate case to avoid any over or under recovery resulting from the COVID-19 pandemic and requested a baseline/benchmark of $0.363 million. Kollen recommended that the Commission reject the proposal stating that the bad debt reserve already tracks the difference in allowed expense compared to write-offs, net of recoveries and there is no need to overlay another deferral mechanism. Atmos Kentucky argued that it is not able to forecast a reasonable bad debt expense and a tracker would balance the needs of the customer and Atmos Kentucky and maintained that, based upon Kollen's

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[94] Atmos Kentucky's Response to the Attorney General's First Request, Item 2(e).

[95] Case No. 2020-00350, *Louisville Gas and Electric Company* (Ky. PSC June 30, 2021), final Order 27-30 (excluding all costs for dues paid to an association where the utility only identified and excluded a specific category of costs related to legislative lobbying from dues it sought to recover in rates).

[96] Case No. 2021-00183, *Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; Issuance of a Certificate of Public Convenience and Necessity; and Other Relief* (Ky. PSC Dec. 28, 2021), Order at 10. Case No. 2021-00185, *Delta* (Ky. PSC Jan. 3, 2022), Order at 8-9.

[97] Atmos Kentucky's response to the Attorney General's First Request, Item 2(c). Atmos Kentucky identified Sam's Club and One Health dues were recorded as social organization dues. These amounts, $310 and $75, respectively, are excluded for the adjustment.

response to Atmos Kentucky's discovery, there is a misunderstanding of what is included in the revenue requirement for bad debt expense and what is recorded for Generally Accepted Accounting Principles (GAAP) purposes.[98] Atmos Kentucky also argued that the Commission's suspension of collections affected its ability to accurately forecast the uncollectible accounts.[99] The Commission's suspension of late payment fees and disconnection for nonpayment was in effect from March 30, 2020 through December 31, 2020, but Atmos Kentucky did not reinstate disconnections or late fees until June 2, 2021.[100]

While the Commission does not agree with Kollen's description of a bad debt reserve as a deferral mechanism in a similar manner to a regulatory asset or liability, the Commission finds that Atmos Kentucky has not established a need for a deferral mechanism due to its inability to forecast uncollectible accounts. Atmos Kentucky forecasted the uncollectible accounts based on its target percentage of 0.50 percent.[101] Requiring ratepayers to shoulder 100 percent of the risk that Atmos Kentucky will experience higher write-offs, while also raising rates, does not "balance the needs of the customer and the Company."[102]

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[98] Christian Rebuttal at 31.

[99] Christian Rebuttal at 31.

[100] Atmos Kentucky's response to Commission Staff's Sixth Request for Information (filed Jan. 6, 2022) (Staff's Sixth Request), Item 6.

[101] Christian Testimony at 36.

[102] Atmos Kentucky's response to Staff's Sixth Request, Item 6(b).

Amortization of Regulatory Liabilities

Atmos Kentucky proposed to temporarily reduce its requested revenue requirement increase by the amortization of regulatory liabilities established in Atmos's last rate case.[103] Atmos Kentucky proposed to return the entirety of the $9.805 million in regulatory liabilities in the first 12 months of the rate increase, for a revenue requirement reduction of $9.862 million.[104] Kollen recommended amortizing the regulatory liabilities to reduce the current increase to $0 until they are exhausted,[105] which at a rate of $1.540 million annually would take approximately 6.4 years.[106]

Out of concern and consideration for increasing energy costs that may exist beyond the short term, the Commission chooses not to amortize the regulatory liabilities to bring the current increase to $0, so that the remaining regulatory asset balances will be available to offset likely or possible increases in energy costs in the foreseeable future, particularly given Atmos Kentucky's history of frequent and periodic rate cases. The Commission finds that a six-year amortization period is reasonable and is approved, which reduces the revenue requirement by $1.644 million. The temporary amortization of regulatory liabilities of $1.644 million shall continue until the regulatory liabilities are exhausted or the effective date of Atmos Kentucky's next base rate case, whichever occurs first.

[103] Christian Testimony at 45.

[104] Christian Testimony at 46.

[105] Kollen Testimony at 4.

[106] Attorney General's Brief at 38. $9.862 / $1.540 = 6.4.

Nonrecurring Charges

As discussed below, the Commission will adjust Atmos Kentucky's nonrecurring charges, which will reduce miscellaneous service charges by $0.126 million and result in a revenue requirement increase of the same amount. The changes to Atmos Kentucky's late payment fees result in an overall reduction in late fee revenue and a revenue requirement increase of $0.997 million.

PRO FORMA ADJUSTMENTS SUMMARY

The effect of the Commission's adjustments on Atmos Kentucky's pro forma test-period operations is as follows:

	Atmos Forecasted Test Period	Commission Accepted Adjustments	Commission Adjusted Test Period
Operating Revenues	$ 173,466,923	$ -	$ 173,466,923
Operating Expenses	144,050,085	(579,584)	143,470,501
Net Operating Income	$ 29,416,838	$ 579,584	$ 29,996,422

RATE OF RETURN

Capital Structure and Cost of Debt

The Kentucky/Mid-States Division of Atmos Energy is not a separate legal entity, and therefore, Atmos Energy issues all debt or equity funding. For ratemaking purposes, the proposed capital structure is equivalent to the Atmos Energy capital structure, excluding the $2.2 billion of financing issued March 2021 due to Winter Storm Uri.[107] The proposed capital structure as of the twelve months ending December 31, 2022, or the end of the forecasted test period, consisted of 42.77 percent long-term debt at a cost of

[107] Christian Testimony, at 54.

4.00 percent; 0.18 percent short-term debt at a cost of 25.17 percent; and 57.05 percent common equity with a proposed ROE of 10.35 percent for a WACC of 7.66 percent.[108] A summary of Atmos Energy's modified cost of capital for Atmos Kentucky follows:

		Percent of Total	Cost Rate	13-month Avg. Cost
Short-Term Debt	$ 21,566,707	0.18%	25.17%	0.05%
Long-Term Debt	$ 5,119,937,524	42.77%	4.00%	1.1%
Common Equity	$ 6,838,047,900	57.05%	10.35%	5.90%
Total Capital	$11,969,542,131			7.66%

In addition to reducing the ROE to 9.10 percent, the Attorney General's witness, Richard A. Baudino, recommended to further modify the capital structure. Regarding the equity ratio of 57.05 percent, Baudino argued that this ratio is unreasonable, unnecessary for the provision of service to its customers, and inflates the revenue requirement and should be rejected.[109] He further noted the Commission's warning in Case No. 2018-00281 about the possibility of reducing the equity ratio if Atmos Kentucky's equity ratio was found to be excessive as compared to that of its peers.[110] Baudino specified that the average equity ratio for the proxy group was 50.30 percent and the common equity ratios requested in recent Kentucky gas rate case filings include 50.695 percent for Duke Kentucky, 52.64 percent for Columbia Gas of Kentucky, and 51.76 percent for Delta Natural Gas.[111] Baudino recommended reducing the equity ratio from 57.05 percent to 53.50 percent, halfway between the proposed amount and the average of the gas proxy

[108] Application, FR_16(8)(j)_Att1_-_Schedule_J.xlsx and Direct Testimony of Dylan W. D'Ascendis (D'Ascendis Testimony), at 3.

[109] Direct Testimony of Richard A Baudino Testimony (Baudino Testimony), at 29.

[110] Baudino Testimony, at 30-31.

[111] Baudino Testimony, at 29 and 30.

group as a first step towards movement to a common equity ratio that is more in line with the proxy groups and, according to Baudino, is more reasonable and affordable for Atmos Kentucky's customers.[112]

For the short-term debt component, the expert witness for the Attorney General, Lane Kollen, averred that the short-term debt capitalization is *de minimis* and unnecessary and yet unreasonably increases the cost of capital and the return on rate base.[113] Kollen maintained that a reasonable level of short-term debt is approximately 2.0 percent of the total capitalization, or at least $240 million, and recommended a transition to the $240 million level by increasing the short-term debt ratio to 1.0 percent, or by $100 million, and to signal an increase to a 2.0 percent short-term debt ratio in the next base rate filing.[114] Kollen also recommended scaling down the commitment fees included in the short-term debt cost rate as the maximum commitment fees for each source of short-term debt is less than half of the fees included in Atmos Kentucky's application, which would result in a lower short-term debt rate.[115]

Finally, regarding the long-term debt component, Kollen proposed to increase the long-term debt component balance by the difference between the decrease in the common equity ratio and the increase in the short-term debt.[116] This shift increases the long-term debt balance $325 million. Kollen further recommended to apply the recent

[112] Baudino Testimony at 31.

[113] Kollen Testimony at 37.

[114] Kollen Testimony at 38.

[115] Kollen Testimony at 38.

[116] Kollen Testimony at 38-39.

cost of new long-term debt of 1.50 percent to this incremental increase.[117] Kollen recognized that his proposed capital structure is hypothetical but averred that the critical factor for the Commission is whether the capital structure is reasonable, not whether it is a forecast or a recent actual capital structure.[118]

Based upon the Attorney General's witnesses' recommendations, the proposed capital structure results in a WACC of 6.65 percent and is as follows:[119]

		Percent of Total	Cost Rate	13-month Avg. Cost
Short-Term Debt	$ 121,556,707	1.02%	2.57%	0.03%
Long-Term Debt	$ 5,444,937,524	45.49%	3.85%	1.75%
Common Equity	$ 6,403,047,900	53.50%	9.10%	4.87%
Total Capital	$11,969,542,131			6.65%

In rebuttal, Atmos Kentucky updated the capital structure through September 2021 to reflect the changes to the balances and cost of debt through the end of the base period. This update included an increase to the common equity ratio from 57.05 percent to 57.59 percent and an increase in the short-term debt rate from 25.17 percent to 80.94 percent. Atmos Kentucky also lowered the short-term debt balance, lowered the long-term debt cost rate to 3.84 percent to reflect recent issuances, and included interest rate swap impacts.[120] The resulting capital structure upon rebuttal is as follows:[121]

[117] Kollen Testimony at 39.

[118] Kollen Testimony at 39-40.

[119] Kollen Testimony at 43.

[120] Atmos Kentucky included interest rate swaps based upon an agreement with the Attorney General for a reduction to rate base for unrealized interest rate swaps if the corresponding adjustment is made to the capital structure. Atmos Kentucky's Response to Staff's Seventh Request for Information (filed Feb. 2, 2022), Item 1.

[121] Christian Rebuttal, Exhibit JTC-R-1-Revised, page 1 of 1.

		Percent of Total	Cost Rate	13-month Avg. Cost
Short-Term Debt	$ 6,704,749	0.05%	80.94%	0.04%
Long-Term Debt	$ 5,717,724,278	42.36%	3.84%	1.63%
Common Equity	$ 7,906,889,837			
Interest Rate Swaps	$ (131,981,063)	57.79%	10.35%	5.96%
Total Capital	$13,499,337,801			7.63%

In response to Baudino's proposed common equity balance, Atmos Kentucky stated that the company uses its actual capital structure as it represents its actual costs and has operated with a capital structure at its current capital structure since Case No. 2018-00281.[122] Atmos Kentucky continued, stating that using the operating subsidiary's capital structure is consistent with the Federal Energy Regulatory Commission's precedent.[123] Atmos Kentucky further argued that to provide safe, reliable, and affordable service to its customers, Atmos Kentucky must meet the needs of its customers, shareholders, and bondholders and safe and reliable service cannot be maintained at a reasonable cost if financial flexibility and strength to access competitive financing markets on reasonable terms does not exist.[124] Atmos Kentucky continued, claiming that a capital structure that understates actual common equity weakens the financial condition of its operation and would have an adverse impact on Atmos Kentucky's ability to address expenses and investment, and it would be a detriment to all stakeholders.[125] Atmos Kentucky stated its capitalization strategy allows Atmos Kentucky the ability to meet its need to accelerate the modernization of its pipeline, which in turn effectively supports the

[122] Christian Rebuttal at 11.

[123] Rebuttal Testimony of Dylan W. D'Ascendis (D'Ascendis Rebuttal) at 55.

[124] D'Ascendis Rebuttal at 55.

[125] D'Ascendis Rebuttal at 55.

long-term safety of its system.[126] Atmos Kentucky further argued that this type of investment is contemplated and encouraged by governing regulation, and thus, results in an increased need to access the capital markets.[127] Further, Atmos Kentucky claimed that in order to maintain Atmos Kentucky's current credit rating, the equity component needs to be in the upper end of the target range for access at the lowest reasonable cost.[128] Atmos Kentucky also argued that although the common equity ratio of 57.59 percent is "somewhat above" the proxy group ratio of 32.15 percent to 52.51 percent, looking at it prospectively, *Value Line Investment Survey's* projected capital structures for the proxy group ranges from 38.50 percent and 57.00 percent for 2024-2026.[129]

Atmos Kentucky argued that both Kollen and Baudino limited their analysis and recommendation to comparison of the proxy group or other recent Commission outcomes and failed to perform an analysis on the financial impact of their recommendations on Atmos Kentucky's own financial metrics.[130] Atmos Kentucky supplied an analysis that key financial indicators are in the Intermediate category, which is the analytical basis for Atmos Kentucky's current debt rating, and both key financial indicators diminish from Intermediate to Significant when Kollen's and Baudino's recommendations are applied.[131] According to Atmos Kentucky, such a change implies that the Kentucky operations would not pull the same weight in the generation of funds from operations or coverage of debt

[126] Christian Revised Rebuttal at 8-9.

[127] Christian Revised Rebuttal at 8.

[128] Christian Revised Rebuttal at 9.

[129] D'Ascendis Rebuttal at 56-57.

[130] Christian Rebuttal at 9.

[131] Christian Rebuttal, at 10 and Exhibit JTC-R-2.

obligations as other Atmos Energy operations, and if Kentucky represented Atmos Energy on the market, higher financing costs would arise.[132]

Regarding the proposed recommendation to increase the short-term debt ratio to 2.0 percent, Atmos Kentucky disagreed with the recommendation and argued that Kollen applied the inverse of his equity argument and employed zero analysis to the increase in the long-term debt ratio, but rather just applied the balance of the recommended equity increase.[133] Atmos Kentucky noted that the company actively accesses the long-term debt market at the benefit of Atmos Kentucky's customers.[134] Atmos Kentucky averred that this activity is not done to minimize short-term debt but rather to lock in lower interest rates and is the result of balance sheet management. Atmos Kentucky did not address the commitment fees in rebuttal.[135]

In his final brief, the Attorney General reemphasized his opinion that the proposed capital structure should be rejected by the Commission as it is beyond traditional norms, unreasonable, and unnecessarily penalizes ratepayers.[136] The Attorney General argued that the proposed common equity ratio is a continuation of several years of ever increasing equity ratios and the Commission should determine a reasonable capital structure.[137] The Attorney General supported Baudino's testimony that the best evidence of a reasonable capital structure is the average for the gas proxy groups and set an equity

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[132] Christian Rebuttal at 10.

[133] Christian Rebuttal at 16

[134] Christian Rebuttal at 17.

[135] Christian Rebuttal at 17.

[136] Attorney General's Brief at 25.

[137] Attorney General's Brief at 26-27.

ratio that represents a two-step transition towards this average.[138] In addition, the Attorney General recommended that the Commission follow Kollen's recommendation regarding the level of short-term and long-term debt balances to further allow for a shift away from the heavily weighted equity component in Atmos Kentucky's capital structure.[139] The Attorney General cautioned the Commission against relying on the exiting capital structure as Atmos Kentucky's choice to utilize common equity financing in lieu of lower cost short-term or long-term financing is not proof that Atmos Kentucky's capital structure is reasonable.[140] Additionally, the Attorney General recommended scaling down the commitment fees, as proposed by Kollen.[141]

Atmos Kentucky noted that a utility's rates should be set to cover operating expenses and the cost of capital.[142] Atmos Kentucky further stated that safety and other infrastructure capital spending is increasing and set by regulatory standards, and, in order to undertake the necessary level of capital investment, Atmos Energy management team, in support of the long-term business strategy to enhance the safety of our customers, has strengthened and maintained Atmos Energy's balance sheet by incorporating a higher level of equity in its capital structure for the benefit of both customers and owners.[143] Atmos Kentucky maintained that the Attorney General has failed to provide any evidence to discredit the use of the current capital structure as he has not put forth any evidence

[138] Attorney General's Brief at 27.

[139] Attorney General's Brief at 28-29.

[140] Attorney General's Brief at 29.

[141] Attorney General's Brief at 30.

[142] Atmos Kentucky's Brief (filed Jan. 14, 2022) at 14.

[143] Atmos Kentucky's Brief at 14-16.

that the management of Atmos Energy has made unsound or imprudent decisions regarding the financing and resulting capital investment, but instead it is a difference in opinion, and thus, the use of the actual capital structure should be allowed.[144] Atmos Kentucky further emphasized the reasonableness of Atmos Kentucky's capital structure, the importance of the relationship between credit metrics and ratings and the cost of capital and cost to Atmos Kentucky's customers, and that the actual capital structure, as filed in Rebuttal, will allow for recovery of all costs during the forecasted test year. Atmos Kentucky noted that the capital structure, as proposed by the Attorney General, is arbitrarily imputed, contains an equity component that is lower than any experienced by Atmos Energy in the recent or forecasted periods, and will result in an under recovery of capital costs during the test year.[145]

Atmos Kentucky admitted to strengthening the equity component and believes that such a strategy benefits Atmos Kentucky's customers, specifically during recent events such as the COVID-19 pandemic, the February 2021 winter event, the implementation of the Tax Cuts and Jobs Act, and the recent tornadoes within Atmos Kentucky's service territory.[146] The table below lists the common equity ratios for Atmos's present and past four rate cases:

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[144] Atmos Kentucky's Brief at 16.

[145] Atmos Kentucky's Brief at 17–18.

[146] Atmos Kentucky's Brief at 15–16.

Case No.	Common Equity Ratio
Pending Case	57.79%
Case No. 2018-00281	58.06%
Case No. 2017-00349[147]	52.57%
Case No. 2015-00343[148]	None Specified
Case No. 2013-00148[149]	49.16%

Additionally, *Value Line Investment Survey* estimates Atmos Energy's common equity ratio balance to reach 60.0 percent over the next four years.[150] In the final Order of Case No. 2018-00281, the Commission voiced its concern over the size of Atmos Kentucky's common equity ratio and agreed with the Attorney General that it was excessive compared to its peers and results in an increase in the cost of capital and base revenue requirement. The Commission accepted the filed equity component but cautioned Atmos Kentucky about the high common equity ratio and placed Atmos Kentucky on notice that in a future rate filing, the Commission may make adjustments to Atmos Kentucky's common equity ratio, for ratemaking purposes, to be comparable to its peers.[151]

In this proceeding, the Commission still has concerns regarding the size of the common equity ratio. Although it is smaller than the prior base rate case, the difference is *de minimis*. The Commission also disagrees with Atmos Kentucky's contention that

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[147] 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 20.

[148] Case No. 2015-00343*, Application of Atmos Energy Corporation for an Adjustment of Rates and Tariff Modifications* (Ky. PSC Aug. 4, 2016).

[149] 7 Case No. 2013-00148, *Application of Atmos Energy Corporation for an Adjustment of Rates and Tariff Modifications* (Ky. PSC Apr. 22, 2014) at 9.

[150] Attorney General's Response to Staff's Second Request for Information (filed Jan. 6, 2022) (Staff's Second Request), Item 4.

[151] Case No. 2018-00281, Order at 34-35.

the equity ratio is within reason of the prospective average for a period of two to four years beyond the end of the forecasted test period.[152] This argument is unsupported as the average for 2022 is expected to be 47.3 percent and 51.9 percent for 2024-2026 projections as compared to 60.0 percent.[153] Additionally, Atmos Kentucky's contention that a high equity component supports government mandates regarding pipe replacement and capital investment is unsupported as its peers who have capital structures containing lower equity components, perform similar capital investments and are required to meet the same safety requirements. Further, Atmos Kentucky's argument that modifying the capital structure applied for ratemaking purposes in Kentucky as proposed by the Attorney General will impact Atmos Energy's debt rates is unsubstantiated. Atmos Kentucky's equity ratio remains significantly higher than its peers for no other reason than for stockholder benefits. The Commission finds that the proposed capital structure as filed and revised upon rebuttal is not reasonable nor does it result in fair and just rates for Kentucky's consumers. The Commission finds Atmos Kentucky's common equity ratio shall be reduced to 54.50 percent. This represents the median for the 2024-2026 prospective period.[154] In addition, in subsequent rate case filings, the Commission will review the proxy group common equity ratios and will further transition down to the average common equity ratio of 50.0 percent or a median or average, whichever the facts merit. The Commission will place the equity balance onto long-term debt at Atmos Kentucky's current average long-term debt rate of 3.84 percent.

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[152] D'Ascendis Rebuttal at 59.

[153] Attorney General's Response to Staff's Second Request, Item 4.

[154] Attorney General's Response to Staff's Second Request, Item 4.

Regarding Kollen's proposed adjustment to the short-term debt balance, the Commission finds that the short-term debt as filed on rebuttal, which represents the capital structure at the end of the base period or September 2021[155] to be reasonable and, although it is uncharacteristically low as compared to the rest of the test year, the Commission chooses to not alter the balance at this time.

Return on Equity

Atmos Kentucky developed its proposed ROE of 10.35 percent based upon the Discounted Cash Flow Model (DCF), the Capital Asset Pricing Model (CAPM), and the Risk Premium Model (RPM) (collectively, Models).[156] In its analysis, Atmos Kentucky used a utility proxy group of seven regulated natural gas utilities (Utility Proxy Group), and a proxy group of forty-eight nonprice regulated companies (Nonprice Regulated Proxy Group).[157] The proxy groups were selected on the basis of several risk measures, including both business risk and financial risk. Additionally, the utility proxy group met a set of criteria in order to remain representative of the risks and prospects faced by Atmos Kentucky.[158] The estimated ROE results ranged from 9.58 percent to 12.66 percent after certain risk adjustments were applied including a size adjustment, risk adjustment and a flotation cost adjustment.[159] Atmos Kentucky averred that the proposed ROE is both commensurate with returns in businesses of similar risks, and captures the continued

[155] Christian Rebuttal at 6.

[156] D'Ascendis Testimony at 3.

[157] D'Ascendis Testimony at 3-4.

[158] D'Ascendis Testimony at 9-12, generally; D'Ascendis Testimony at 12-13. *See* also Atmos Kentucky's Responses to Staff's Second Request, item 36c.

[159] D'Ascendis Testimony at 3-4, lines 13-18 and 1-2, respectively, and Table 2 at 4.

uncertainty related to the COVID-19 pandemic and the unknown timeframe for when economic conditions will normalize.[160] Atmos Kentucky maintained that the use of multiple models adds reliability to the estimated common equity cost rate, and is supported in both the financial literature and by regulatory precedent.[161] No reduction to Atmos Kentucky's capital cost recovery rider, the PRP was proposed. The estimated ROE results plus the three adjustments are shown below.[162]

Atmos Kentucky's Cost of Common Equity Rates	
Discounted Cash Flow Model	9.44%
Risk Premium Model	10.96%
Capital Asset Pricing Model	11.75%
Cost of Equity Models Applied to Comparable Risk, Non-Price Regulated Companies	12.42%
Indicated Range	9.44% - 12.42%
Size Adjustment	0.20%
Credit Risk Adjustment	-0.10%
Flotation Cost Adjustment	0.04%
Recommended Range	9.58% - 12.66%
Recommended Cost of Common Equity	10.35%

Direct intervenor testimony and analysis regarding ROE was sponsored by the Attorney General and performed by Richard A. Baudino. Baudino's analysis used the DCF and the CAPM model. Using a proxy group of seven regulated natural gas distribution companies, and the DCF model only, a ROE range of 8.40 percent to 9.40

[160] D'Ascendis Testimony at 4-7.

[161] D'Ascendis Testimony at 42.

[162] D'Ascendis Testimony Table 2 at 4.

percent was obtained.[163] For the CAPM analysis, Baudino evaluated both historical and forecasted risk premiums as an alternative method to calculate ROE stating the belief that the CAPM is less reliable than the DCF because considerable judgement must be employed to determine market returns and expected risk premium elements and analyst's judgement can influence the results significantly.[164] In addition, Baudino recommended that the Commission consider a 10-20 basis point reduction in the allowed ROE for Atmos Kentucky's PRP rider.[165] The following table summarizes the Attorney General's results:[166]

Attorney General Cost of Common Equity Rates	
Discounted Cash Flow Model	
Average Growth Rates	
High	10.81%
Low	8.42%
Average	9.49%
Median Growth Rates	
High	10.60%
Low	8.05%
Average	9.20%
CAPM Methodology	
Forward-looking Market Return	
Current 30-year Treasury	8.69%
D&P Normal Risk-Free Rate	8.73%
Historical Risk Premium	
Current 30-year Treasury	7.56% - 8.73%
D&P Normal Risk-Free Rate	7.90% - 9.07%

[163] Baudino Testimony at 3, 17, and 28.

[164] Baudino Testimony at 3, 15, and 23-24.

[165] Baudino Testimony at 3 and 32-34.

[166] Baudino Testimony at 28.

Baudino argued that his recommended ROE is reasonable given the lower risk of the regulated gas business as compared to the regulated electric business, and that it is consistent with investor expectations and requirements in the current economic environment of low interest rates.[167] In addition, the CAPM ROE estimates are generally below the DCF estimates, which further supports the reasonableness of the recommended ROE.[168] Baudino also referred to *Value Line Investments* statements regarding the natural gas distribution sector indicated that that it was providing a consistent income stream to investors with relatively stable earnings, which indicates that the proxy group had lower risk than the overall stock market.[169]

Baudino took issue with multiple assumptions used in Atmos Kentucky's ROE calculations and concluded that its 10.35 percent recommendation was inconsistent with current financial market evidence and the low interest rate environment.[170] In addition, Baudino argued that D'Ascendis's approach to reach his recommended ROE was unreasonable and stemmed from excessively high ROE results from his risk premium and CAPM analyses as well as the inclusion of an additional proxy group of 48 non-price regulated companies.[171] Baudino also noted that an ROE of 10.35 greatly exceeds recent Commission ROE awards.[172]

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[167] Baudino Testimony at 3

[168] Baudino Testimony at 3.

[169] Baudino Testimony at 15.

[170] Baudino Testimony at 11-15 and 35.

[171] Baudino Testimony at 36.

[172] Baudino Testimony at 37.

Regarding D'Ascendis's DCF calculations, Baudino argued that in addition to using earnings growth rates, dividend growth rates should have been included because dividend payments comprise a significant portion of the total return to investors.[173] Regarding the Risk Premium (RP) analyses, Baudino argued that they are too imprecise and should only be used as a guide for estimating ROEs in regulated proceedings.[174] Regarding the Predictive Risk Premium Model (PRPM) and the total market RP approaches, Baudino claimed that D'Ascendis failed to consider current bond yields and interest rates, which led to unrealistically high ROEs.[175] Concerning the PRPM, Baudino argued that it should be rejected because it is unproven, and not widely accepted. Baudino also noted it had been rejected by the Florida Public Service Commission and argued that it produces excessive ROE results.[176] Regarding the CAPM and ECAPM analyses, the Attorney General argued that Atmos's CAPM and ECAPM results, which are based on overstated expected market returns and long-term growth rates, are so overstated for a regulated gas utility that they should be rejected out of hand.[177] In addition, Baudino maintained that the use of the ECAPM to correct for companies with betas less than 1.0 is another indication that the model is not sufficiently accurate and the use of unregulated companies as proxies for a regulated company is inappropriate.[178]

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[173] Baudino Testimony at 37-38.

[174] Baudino Testimony at 38.

[175] Baudino Testimony at 38-42.

[176] Baudino Testimony at 42-44.

[177] Baudino Testimony at 45-48.

[178] Baudino Testimony at 50-51.

Finally, Baudinio argued that the inclusion of size adjustments and flotation cost adjustments is inappropriate and should be rejected.[179]

In rebuttal, Atmos Kentucky argued that Baudino's original ROE recommendation of 10.35 percent for its base rates remains both reasonable and conservative.[180] In addition, Atmos Kentucky provided an updated ROE analysis using the same methods and updated data as of September 30, 2021, which illustrated an even higher ROE range.[181]

Atmos Kentucky discussed several issues found in Baudino's analysis including the exclusive reliance on the constant growth DCF model results to determine his recommended ROE.[182] Atmos Kentucky implied that the absence of multiple models in the Attorney General's analysis reduces the reliability of the estimated common equity cost rate.[183] Further, Atmos Kentucky argued that the DCF assumes a Market-to-Book (M/B) ratio of 1.0 and is prone to either under or over-estimate investors' required returns when a disparity exists.[184] In addition, Atmos Kentucky argued that the use of earnings per share growth rates is more appropriate in DCF analyses than the use of dividends per share growth rates.[185] Atmos Kentucky also found fault with Baudino's CAPM analysis reliance on a recent six month average of the 30-year Treasury bond yield as

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[179] Baudino Testimony at 38-42.

[180] D'Ascendis Rebuttal at 2.

[181] D'Ascendis Rebuttal at 2.

[182] D'Ascendis Rebuttal at 4.

[183] D'Ascendis Rebuttal at 4.

[184] D'Ascendis Rebuttal at 7.

[185] D'Ascendis Rebuttal at 12.

the risk free rate, failure to consider several approaches to calculating the market risk premium, and failure to incorporate the empirical CAPM analysis to correct for low-beta values.[186]

In its brief, Atmos Kentucky reiterated arguments put forth by D'Ascendis that the ROE should be sufficient to support both the business and financial risk of the company on a stand-alone basis.[187] The DCF model, the Risk Premium Method, the PRPM and CAPM models all utilize market data. Atmos Kentucky argued that it is appropriate to rely on multiple model results because reasonable investors use a variety of tools and do not rely exclusively on a single information source or model.[188] Reliance on multiple models adds reliability to estimated common equity rates and is supported by both financial literature and regulatory prudence.[189] Atmos Kentucky argued for and defended its use of size adjustments and flotation costs in arriving at its 10.35 percent recommendation. Critiquing Baudino's analyses, Atmos Kentucky argued that only the DCF and CAPM models were used, the analyses were flawed and only the DCF results were relied upon as the basis for his ROE recommendation.[190] Finally, Baudino failed to use the Empirical CAPM to account for low beta valued securities.[191]

In his brief, the Attorney General argued that Baudino's recommended 9.10 percent ROE is reasonable given the low risk nature of Atmos Kentucky's regulated gas

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[186] D'Ascendis Rebuttal at 23-24.

[187] Atmos Kentucky's Brief at 16.

[188] Atmos Kentucky's Brief at 18-19.

[189] Atmos Kentucky's Brief at 19.

[190] Atmos Kentucky's Brief at 21.

[191] Atmos Kentucky's Brief at 22.

business and it's consistent with investor expectations and requirements in the current economic environment of low interest rates.[192] Baudino utilized both the DCF and CAPM models with both historical and forecasted data from multiple sources and the same utility proxy group as D'Ascendis.[193] The recommendation is based upon the DCF results only because the CAPM results were generally lower than the DCFR results. Further, the CAPM model is a less reliable approach than the DCF model.[194] Based on recent precedent, Baudino recommended a 10-20 basis point ROE reduction for Atmos Kentucky's PRP rider.[195] The Attorney General argued that D'Ascendis' ROE analyses results were so high that they should not be seriously considered for a lower risk regulated gas distribution utility.[196] In addition, there were flaws in the DCF, CAPM and RPM model analyses, the use of ECAPM is suspect, the use of non-price regulated companies as proxies, and the use of the PRPM model is inappropriate. Finally, the use of size adjustments, and financial adjustments are inappropriate and have been rejected by this Commission in recent cases.[197]

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[192] Attorney General Brief at 32.

[193] Attorney General Brief at 31.

[194] Attorney General Brief at 31.

[195] Attorney General Brief at 33.

[196] Attorney General Brief at 34.

[197] Attorney General Brief at 34–37.

Most recently in Case Nos. 2021-00183,[198] 2021-00185,[199] and 2021-00190,[200] the Commission explained why it is appropriate for utilities to present, and for the Commission to evaluate, multiple methodologies to estimate ROEs. Each approach has its own strengths and limiting assumptions. As demonstrated in the respective ROE testimonies in this proceeding, there is considerable variation in both data and application within each modeling approach, which can lead to very different results. The Commission's role is to conduct a balanced analysis of all presented models, while giving weight to current economic conditions and trends.

The Commission cautions all parties against unreasonably removing or ignoring "outlier" data due to a subjective perception of being "too high" or "too low." As demonstrated in the case record, there are a number of actions that can be and were taken to account for "outlier" or "unreasonable" data. Result oriented exclusions of data that are not beyond the realm of reasonableness are inappropriate. Results based upon excluded data without adequate support will be given less weight in future Commission determinations.

Even though the Commission supports the use and presentation of multiple modeling approaches, the Commission finds that Atmos Kentucky's use of the Predictive Risk Premium Model (PRPM) should be rejected. Though the PRPM model has been

[198] *See* generally Case No. 2021-00183, *Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; Issuance of a Certificate of Public Convenience and Necessity; And Other Relief* (Ky. PSC Dec. 28, 2021).

[199] *See* generally Case No. 2021-00185, *Electronic Application of Delta Natural Gas Company, Inc. for an Adjustment if Its Rates and a Certificate of Public Convenience and Necessity* (Ky. PSC Jan. 3, 2022).

[200] *See* generally Case No. 2021-00190, *Electronic Application of Duke Energy Kentucky, Inc. for: 1) An Adjustment of the Natural Gas Rates; 2) Approval of New Tariffs, And 3) All Other Required Approvals, Waivers, and Relief* (Ky. PSC Jan. 28, 2021).

published and presented in multiple forums, it has been rejected by this Commission and only been addressed by three other regulatory commissions thus far and is not universally accepted.[201]

The Commission reiterates that it continues to reject the use of flotation cost adjustments, financial risk adjustments, and size adjustments in the ROE analyses. The Commission will evaluate all models but will accord most weight to DCF and CAPM analyses based upon regulated company proxy groups. Both the DCF and CAPM are long standing, well accepted models that model risk and returns both implicitly and explicitly. After consideration of the evidence of record, the Commission finds that an ROE of 9.23 percent for Atmos Kentucky's base rates and an ROE of 9.13 percent for its natural gas capital riders is fair, just and reasonable. An ROE of 9.23 percent is lower than recent Commission awards for gas utilities, but those awards were tied to stay-out provisions or for a utility that is significantly smaller, rural and had not requested a rate increase for over ten years. Additionally, in deciding upon the approved ROE, the Commission is also balancing the recent destruction due to the devastating tornados and customer bill impact during the region's recovery, as well as the still high equity percentage.

<u>Rate-of-Return Summary</u>

Applying the cost rates of 80.94 percent for short-term debt, 3.84 percent for long-term debt, and 9.23 for common equity to the Commission revised capital structure

[201] *See* the Final Order in Case No. 2021-00183 ((Ky. PSC Dec. 28, 2021) at 14 and Atmos Kentucky's Response to the Attorney General's First Request for Information, Item 66b, filed Aug 23, 2021.

percentages consisting of 0.05 percent, 45.45 percent, and 54.50 percent, respectively, produces and overall weighted cost of capital of 6.82 percent.

		Percent of Total	Cost Rate	13-month Avg. Cost
Short-Term Debt	$ 6,704,749	0.05%	80.94%	0.04%
Long-Term Debt	$ 6,135,493,495	45.45%	3.84%	1.73%
Common Equity	$ 7,489,119,620			
Interest Rate Swaps[202]	$ (131,981,063)	54.50%	9.23%	5.03%
Total Capital	$13,499,337,801			6.82%

REVENUE REQUIREMENTS

Based upon Atmos Kentucky's revised requested increase of $15.052 million and recognizing downward adjustments of $10.796 million found reasonable herein,[203] Atmos Kentucky's revenue deficiency is $4.256 million. As discussed above, temporary amortization of regulatory liabilities of $1.644 million shall continue until the regulatory liabilities are exhausted or the effective date of Atmos Kentucky's next base rate case, whichever comes first. The resulting net increase to base rates is $2.613 million or 1.51 percent.

RATE DESIGN

Cost of Service Study (COSS)

Atmos Kentucky filed three fully allocated cost of service studies (COSS). For all three studies, the demand allocators are based upon the demand to meet the coincident peak. For the allocation of the distribution mains, the Customer/Demand Study, allocated

[202] Atmos Kentucky included interest rate swaps based upon an agreement with the Attorney General for a reduction to rate base for unrealized interest rate swaps if the corresponding adjustment is made to the capital structure. Atmos Kentucky's Response to Staff's Seventh Request for Information, Item 1.

[203] *See* Appendix A to this Order for a summary of adjustments.

the distribution mains between customer and demand costs based upon the minimum system method, as the zero-intercept method failed. For the Demand Only Study, the distribution mains were allocated based upon demand only. Finally, Atmos Kentucky performed a Demand/Commodity Study based upon the average and excess methodology where consideration is focused on volume of use. The Attorney General's Testimony did not address Atmos Kentucky's COSSs and did not propose an alternate COSS.

<u>Revenue Allocation</u>

For the revenue allocation, Atmos Kentucky examined the minimum and maximum subsidy that existed between each class at the proposed rate of return (ROR) from each COSS and roughly allocated the revenue based on the average revenue increase between the three COSSs necessary for an equalized ROR.[204] As a result, the residential class received over 59 percent of the increase. Below illustrates the relative ROR at current rates and at Atmos Kentucky's proposed rates:

	Residential	Non-Res Firm	Non-Res Inter	Trans Firm	Trans Inter
Customer/Demand[205]					
Current	0.74	1.45	1.26	1.65	1.54
Proposed	0.80	1.41	1.43	1.42	1.36
Demand Only[206]					
Current	1.05	1.10	0.42	0.78	0.71
Proposed	1.05	1.11	0.63	0.75	0.71
Demand/Commodity[207]					
Current	1.22	1.24	0.18	0.44	0.22
Proposed	1.19	1.22	0.42	0.49	0.33

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[204] Application, Direct Testimony of Paul H. Raab (Raab Testimony) at 20, and Exhibit PHR-5, page 2 of 2.

[205] Raab Testimony, Exhibit PHR-2, page 1 of 75.

[206] Raab Testimony, Exhibit PHR-3, page 1 of 75.

[207] Rabb Testimony, Exhibit PHR-4, page 1 of 75.

The Commission has expressed its concern about the demand/customer expense allocation for distribution plant classification and the Commission's preference for the zero-intercept method.[208] Although this concern has been expressed in electric rate cases, it was also recently expressed for natural gas[209] as the same concept applies to natural gas in that if the zero-intercept analysis does not provide reasonable results, then this indicates little relationship between the amount of costs and the number of customers. The Commission gives substantial weight to the evidence from the COSS that indicates whether certain classes are earning more than other rate classes relative to their cost of service and has required that in instances where the zero-intercept results are not reasonable, it would allocate the costs to 100 percent demand.

For the reasons set forth above regarding the deficiencies of using a minimum system method, the Commission rejects the Customer Demand Study. The Commission approves the use of the Demand Only Study as a guide for revenue allocation and rate design. The results of the Demand Only Study illustrate that the residential class is slightly subsidizing other rate classes. However, due to the tie between the volumetric rates for the G-1 Firm Sales Service and Transportation Service and the G-2 Interruptible Sales Service and T-3 Interruptible Transportation, removing the subsidization in the residential class results in a rate design that diverges far too much from the current rate design. Therefore, the Commission shall allocate the change in revenue as approved herein proportionally, as filed.

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[208] *See*, Case No. 2020-00131, Electronic Application of Meade County Rural Electric Cooperative Corporation for an Adjustment in Rates (Ky. PSC Sept. 16, 2020), Order at 12.

[209] *See*, Case No. 2021-00190, *Electric Application of Duke Energy Kentucky, Inc. for: 1) an Adjustment of Natural Gas Rates; 2) Approval of New Tariffs, and 3) All other Required Approvals, Waivers, and Relief* (Ky. PSC Jan 25, 2022).

Rate Design

Atmos Kentucky proposed no change in rate design, maintaining a monthly base customer charge and declining block volumetric rates for all rate schedules. It proposed to increase the G-1 Firm Sales Service base customer charge to $24.29 for residential customers, revised to $24.00 on rebuttal, and to $66.00 for non-residential customers. In the last five years, the residential customer charge has increased from $16.00 to the current charge of $19.30. The current residential customer charges among Kentucky's large gas utilities include $19.50 for Louisville Gas and Electric,[210] $19.75 for Columbia Gas of Kentucky,[211] and $17.50 for Duke Energy Kentucky.[212]

The Attorney General argued that Atmos Kentucky has not presented any evidence that the current customer charge is insufficient for the company to meet its revenue requirement, nor does the increase support the principles of rate gradualism.[213] He continued stating that this proposed increase comes at a time when customers in Atmos Kentucky's service territory are recovering from a devastating natural disaster as

[210] *See*, Case No. 2020-00350, *Electronic Application of Louisville Gas and Electric Company for an Adjustment of Its Electric and Gas Rages, a Certificate of Public Convenience and Necessity to Deploy Advanced Metering Infrastructure, Approval of Certain Regulatory and Accounting Treatments, and Establishment of a One-Year Surcredit* (Ky. PSC Dec. 6, 2021), Appendix C, page 8 of 10. $0.65*30=$19.50.

[211] *See*, Case No. 2021-00183, Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; Issuance of a Certificate of Public Convenience and Necessity; and Other Relief (Ky. PAS Dec. 29, 2021), Appendix B, page 1 of 1.

[212] *See*, Case No. 2021-00190, Dec. 28, 2021 Order, Appendix C, page 1 of 1.

[213] Attorney General's Brief at 43.

well as seeing a 23 percent increase in the gas commodity cost.[214] Therefore, the Attorney General urged the Commission to evaluate the totality of the rate increase.[215]

The proposed residential customer charge increase, if approved, will result in Atmos Kentucky being one of the most expensive customer charges in the Commonwealth. Further, the Commission agrees that given the recent natural disaster and increases in commodity costs, thoughtful consideration needs to be given to the totality of the rate increase. Therefore, the Commission is denying the increase to the Residential Sales monthly customer charge and finds that the monthly charge shall remain at $19.30. The Commission further finds that the proposed customer charges for the remaining rate classes are within the range of reasonableness and are approved.

Nonrecurring Charge Forecast

For the late payment charge revenue forecast, Atmos Kentucky used an average of fiscal years 2017–2019 to determine forecasted late payment charges. For its other nonrecurring charges, Atmos Kentucky used the actual for the 12 months ending March 31, 2021, to forecast its nonrecurring charge revenue.[216] Atmos Kentucky argued that based upon a review of the impacts of COVID-19, it has seen that the reduction in revenue has been offset by a reduction in O&M expenses.[217] Atmos Kentucky stated that due to the uncertainty of when nonrecurring charges will return to a normal level, they chose not to make any changes to other nonrecurring charge revenue and that the reduced revenue

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[214] Attorney General's Brief at 43.

[215] Attorney General's Brief at 43.

[216] Atmos Kentucky's response to Commission Staff's Second Request, Item 54(a).

[217] Atmos Kentucky's response to Commission Staff's Second Request, Item 54(b).

and O&M expenses will continue to offset each other.[218] As Atmos Kentucky used an average of fiscal years 2017–2019 to forecast its late payment fee revenues, the Commission finds that the same time period should be used to forecast other nonrecurring charge revenues. Based upon the revised period used to forecast revenues and the revisions to nonrecurring charges discussed later in this order, the amount of forecasted nonrecurring charge revenue is reduced from $234,286 to $108,769 as detailed below.

Charge	FY 2017-2019 Avg. Occurrences	Approved Amount	Total Revenue	Forecasted Revenue	Difference
Read (Reg)	13,113	$3.00	$39,339.00	$136,968.00	($97,629.00)
Meter Set (Reg)	2,505	3.00	7,515.00	36,550.00	(29,035.00)
Meter Set (After)	1	44.00	44.00	0.00	44.00
Seasonal (Reg)	282	3.00	846.00	195.00	651.00
Ret. Check	3,126	4.00	12,504.00	54,800.00	(42,296.00)
Rec. Del. (Reg)	3,932	3.00	11,796.00	0.00	11,796.00
Rec. Del. (After)	1	47.00	47.00	0.00	47.00
Turn-On (Reg)	12,170	3.00	36,510.00	5,773.00	30,737.00
Turn-On (After)	6	28.00	168.00	0.00	168.00
			$108,769.00	$234,286.00	($125,517.00)

As a result, an increase to the Revenue Requirement for base rates that corresponds with an equivalent decrease in Nonrecurring Charge Revenue is necessary.

Late Payment Fee Revenue

Information provided by Atmos Kentucky indicated that for fiscal years 2017-2019, the percent of late payment fee revenue to total revenue from Commercial and Public Authority customers was 0.63 percent and 0.55 percent, respectively.[219] To determine the appropriate amount of late payment fee revenue, the Commission determined the

[218] Atmos Kentucky's response to Commission Staff's Second Request, Item 54(b).

[219] Atmos Kentucky's response to Commission Staff's Second Request, Item 26, Attachment 2.

amount of revenue to be derived from Commercial and Public Authority customers as a result of the revised revenue requirement and multiplied those amounts by 0.63 percent and 0.55 percent. Based on the calculation described above and the removal of the residential late payment fee discussed later in this order, the Commission determined that late payment fee revenue should be reduced by $0.997 million, $0.874 million being attributable to the removal of residential late payment fees and $0.123 million being attributable to the reduction in commercial and public authority late payment fees. As a result, an increase to the Revenue Requirement for base rates that corresponds with an equivalent decrease in late payment fee revenue is necessary. A chart containing a summary of the revenue requirement, as proposed by Atmos Kentucky and as modified herein, is attached to this Order as Appendix A.

PIPE REPLACEMENT PROGRAM

Aldyl-A Replacement Projects

Atmos Kentucky proposed to expand its current PRP to include the accelerated replacement of Aldyl-A pipe. Atmos Kentucky stated that Aldyl-A pipe is made of materials that are considered obsolete and are no longer used and places risks on Atmos Kentucky's distribution system, which contains approximately 205 miles of Aldyl-A pipe.[220] Atmos Kentucky stated that leaks on Aldyl-A average 35 percent higher per 100 miles than leaks on other types of polyethylene pipe and 250 percent higher per 100 mile of pipe when compared with leaks on coated steel pipes.[221] Atmos Kentucky noted that not all Aldyl-A needs to be replaced immediately, and will prioritize replacement based upon

[220] Direct Testimony of T. Ryan Austin (Austin Testimony) at 23.

[221] Austin Testimony at 25-26.

material, location of the pipe in relation to population, and relative risk from third party damage.[222] Atmos Kentucky proposed to target Cadiz, Kentucky (Cadiz Project), first as this portion of the system has had a history of leaks caused by the rocky bedding conditions impinging on the Aldyl-A pipe, at a forecasted test year cost of $2.794 million.[223]

Kollen recommended that the Commission reject the inclusion of Aldyl-A in the PRP because there is no imminent need to replace this material.[224] Kollen argued that Atmos Kentucky's bare steel replacement program will not be complete until 2027, and the accelerated replacement of Aldyl-A would compound the annual rate base increase.[225] Kollen noted that Atmos Kentucky failed to provide a schedule or cost estimate to completely replace all Aldyl-A pipe.[226] Kollen recommended that the Commission allow the proposed incremental accelerated Aldyl-A replacement costs be included in the base revenue requirement, and if Atmos Kentucky does not complete the projects included in the base revenue requirement, apply a clawback of the related base revenues.[227] Additionally, Kollen recommended that Atmos Kentucky be required to file reports with the Commission following project completion, and, if the project was not

[222] Austin Testimony at 27.

[223] Austin Testimony at 28-29.

[224] Kollen Testimony at 44.

[225] Kollen Testimony at 44-45.

[226] Kollen Testimony at 45.

[227] Kollen Testimony at 46.

complete, the clawback revenue total and to record this revenue as a regulatory liability for disposition in the next base rate case.[228]

Atmos Kentucky argued that Kollen's position is inconsistent with the Attorney General's position in Columbia Kentucky's rate case, Case No. 2021-00183,[229] where the Attorney General's witness, David Dittemore, recommended the inclusion of Aldyl-A replacement pipe in Columbia Kentucky's Safety Modification and Replacement Program rider.[230] Atmos Kentucky stated it has identified Aldyl-A projects for replacement for two years and is able to estimate the number of years necessary to replace the Aldyl-A inventory.[231] Atmos Kentucky disagreed with Kollen's proposal to include accelerated Aldyl-A replacement in the base revenue requirement stating it is not a comprehensive solution.[232] Atmos Kentucky stated that Aldyl-A replacement is necessary for safety and reliability and because Atmos's non-PRP capital spend is also subject to an annual cap, such constraints may result in Aldyl-A replacement not occurring outside of the PRP.[233] Atmos Kentucky maintained excluding Aldyl-A from recovery on capital spend constrains investment associated with economic development and growth.[234] Atmos Kentucky argued that since its last rate case, there is a new emphasis by federal regulators to

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[228] Kollen Testimony at 46-47.

[229] Case No. 2021-00183, *Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; Issuance of a Certificate of Public Convenience and Necessity; and Other Relief* (Ky. PSC Dec. 28, 2021).

[230] Rebuttal Testimony of T. Ryan Austin (Austin Rebuttal) at 3 and Atmos Kentucky's Final Brief at 35.

[231] Austin Rebuttal at 8.

[232] Austin Rebuttal at 9.

[233] Austin Rebuttal at 2, Christian Rebuttal at 35m and Atmos Kentucky's Brief at 34.

[234] Christian Rebuttal at 35 and Atmos Kentucky's Brief at 40.

address pipeline safety, particularly Aldyl-A, and utilities must have appropriate replacement cycles for all pipeline infrastructure.[235] Atmos Kentucky stated that Kollen ignored the need to modify the PRP tariff to enhance safety concerns and instead focused on cost concerns.[236] Atmos Kentucky admitted that the existence of the PRP does reduce lag and supports Atmos Kentucky's credit health, but there are also customer benefits including safer service, more affordable service, and more reliable service thus striking a balance between the customer and Atmos Kentucky.[237]

The Attorney General again reiterated that there is no immediate need to replace the Aldyl-A pipes, and noted that this is something that Atmos Kentucky itself acknowledged.[238] The Attorney General argued that the lack of a schedule, cost estimate, and annual or aggregate cost limits would allow for unchecked spending, which is concerning as the Commission has had to caution Atmos Kentucky about excessive spending in the past.[239] The Attorney General noted that the Commission recently rejected the inclusion of accelerated replacement and cost recovery of Aldyl-A for Columbia Kentucky and should likewise reject Atmos Kentucky's proposal.[240] The Attorney General did recommend the inclusion of Aldyl-A replacement costs in the base

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[235] Atmos Kentucky's Brief at 27 and 29.

[236] Atmos Kentucky's Brief at 35.

[237] Atmos Kentucky's Brief at 37.

[238] Attorney General's Brief at 38.

[239] Attorney General's Brief at 39-40.

[240] Attorney General's Brief at 40.

revenue requirement, but reiterated Kollen's suggestion regarding the clawback of any costs not spent.[241]

As required by PRP tariff, the impact of Atmos Kentucky's PRP investment is reflected in the total proposed revenue requirement. Per the PRP tariff, Atmos Kentucky filed Case No. 2021-00304 in August which included Atmos Kentucky's forecasted spend between October 1, 2021, and September 30, 2022, of $27.9 million.[242] Due to the instant case, the Commission suspended Case No. 2021-00304 pending the results of this case. Atmos Kentucky has proposed to include the forecasted spend in base rates and reset the PRP to $0 through September 2022.

Atmos Kentucky's below ground leaks have decreased from 18.83 per 100 miles to 14.11 per 100 miles between 2016 and 2020. However, below ground leaks associated with bare steel has remained rather constant between 2016 and 2020 at 45.76 per 100 miles and 47.69 leaks per 100 miles, respectively, whereas below ground leaks for Aldyl-A pipe has fallen from a high of 35.47 leaks per 100 miles in 2016 to 27.21 leaks per 100 miles in 2020.[243] Although a concern, plastic pipe is not a safety issue that is on the same magnitude as bare steel, which is still on the system to be replaced. Further, although Aldyl-A pipe is a risk, Aldyl-A materials and other industry identified vintage plastics are considered to be a sub-threat and Aldyl-A represents only approximately 5.00 percent of Atmos Kentucky's total system.[244] Therefore, the Commission finds that Atmos

[241] Attorney General's Brief at 40.

[242] Case No. 2021-00304, *Electronic Application of Atmos Energy Corporation to Establish PRP Rider Rates for the Twelve Month Period Beginning October 1, 2021* (Ky. PSC filed July 30, 2021).

[243] Atmos Kentucky's Response to Staff's Second Request, Item 31.

[244]Atmos Kentucky's Response to Staff's Second Request, Items 30 and 31.

Kentucky's proposal to include Aldyl-A pipe in its PRP is denied. The inclusion of future Aldyl-A pipelines will be determined on a case by cases basis and any PRP applications including Aldyl-A projects should at minimum include safety justifications for such projects. The Commission approves of the inclusion of the $2.794 million for the Cadiz Project in the test year revenue requirement.

The Commission reminds Atmos Kentucky that the purpose of a rider tied to capital investment in the natural gas industry is to address specific problems such as bare steel or a section of pipe prone to issues and may be tied to specific directives issued by Pipeline and Hazardous Materials Safety Administration. The Commission also notes that in its application, Atmos Kentucky stated the PRP allows the Company to extend the period between base rate cases yet Atmos has filed 6 rate cases since the PRP was implemented in 2011.[245] Not including certain projects in the PRP nor capping the PRP has not slowed down Atmos's capital investment, as evident in the increase in Atmos Kentucky's rate base of $180.645 million in for the base period ending 2009 when the PRP was first approved[246] to $568.506 million, an almost 215 percent increase, or an average of 14 percent annually over the last 15 years. Of course, this increase in rate base requires higher rates that reflect a return of and on the investment. Essentially, Atmos Kentucky has more than doubled the amount of money it makes from Kentuckians in less than 15 years.

The Commission approves the roll-in of the PRP into base rates in this preceding. However, the Commission instructs Atmos Kentucky to alter the PRP from a per meter

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[245] Direct Testimony of Brannon C. Taylor (Taylor Testimony) at 7.

[246] Case No. 2009-000354, *Application of Atmos Energy Corporation for an Adjustment of Rates* (KY. PSC May 28, 2010), Volume 6, FR 10(10)(b)

charge to a volumetric charge moving forward. The Commission recognizes that capital spending is Atmos Kentucky's greatest expense and believes depicting the PRP and its associated spending as a separate line item on customer bills allows for greater transparency. Therefore, in Atmos Kentucky's next base rate case, Atmos Kentucky is to file testimony demonstrating why the rider should be rolled-in to base rates. The Commission also requests that Atmos Kentucky maintain distinct records where costs are delineated so that the percent resulting from rehabilitation to meet standards established by city and municipal governments and to work with local governments to lower these expenses.

<u>NOL ADIT</u>

Kollen argued that Atmos Energy's NOL position is reversing so it is no longer reasonable to assume that the PRP will generate incremental NOL ADIT to completely offset incremental liability ADIT.[247] Therefore, Kollen recommended modifying the PRP calculation to reflect that asset NOL ADIT is not generated incrementally by the PRP spend or require Atmos Kentucky to include the actual impacts on the NOL ADIT in the PRP.[248]

Atmos Kentucky argued that the amount of asset NOL ADIT included in rate base and the PRP Rider is appropriate and should not be adjusted and the PRP ADIT treatment is reasonable given base period results.[249]

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[247] Kollen Testimony at 48.

[248] Kollen Testimony at 48-49.

[249] Rebuttal Testimony of Joel J. Multer at 10-11.

The Attorney General and Kollen's position is that Atmos Kentucky inappropriately offsets and reduces the incremental liability ADIT due to accelerated tax deprecation subtracted from rate base by the incremental asset NOL ADIT.[250]

The Commission agrees, in part, with Kollen's recommendations regarding the treatment of NOL ADIT in the PRP. Specifically, consistent with the Commission's determination above that the generation and utilization of NOL ADIT included in rate base for Kentucky should be based on Kentucky operations, the PRP calculation should only reflect an incremental increase in NOL ADIT if Atmos Kentucky is able to establish that its Kentucky operations and its PRP spend actually generated NOL ADIT during the relevant period. The Commission will not accept the imputation of NOL ADIT where none was generated by Kentucky operations in the PRP period, because it would be inconsistent with ratemaking principles and federal normalization rules.[251] However, Atmos Kentucky's current tariff requires the PRP Revenue Requirement to be calculated using the "PRP-related Plant In-Service not included in base gas rates minus the associated PRP-related accumulated depreciation and accumulated deferred income taxes,"[252] which would not require the Commission to impute NOL ADIT where none

[250] Attorney General's Brief at 40.

[251] *See Matter of Missouri-American Water Company*, 637 S.W.3d 121, 127-8 (MP App. 2021)(The court rejected Missouri-American Water Company's calculation of NOL ADIT in a pipeline replacement rider based solely on a comparison of the ADIT generated from the pipeline replacement spend and the gross income from the pipeline replacement rider; noted that a pipeline replacement program would always generate NOL ADIT using that method; and found that the calculation of the NOL ADIT generated should be based on the gross income from all operations in the state during the relevant period); *see also* Private Letter Ruling 113227-19, 2020 WL 1071276 (issued Dec. 3, 2019) (finding, among other things, that book-tax timing differences arising from repairs, which now make up the bulk of the book-tax timing differences in Atmos's PRP, are not subject to normalization rules); 26 C.F.R. § 1.167(l)-1(h)(1)(i) (requiring a utility's reserve for deferred taxes to reflect the total amount of the deferral of federal income tax liability resulting from the taxpayer's use of accelerated depreciation).

[252] Application, Attachment 1, PSC KY. No. 2, Fourth Revised SHEET No. 38.

exists.[253] Thus, the Commission finds that it is not necessary to amend the language of the PRP tariff and the specific calculation of NOL ADIT in the PRP, if any, will be addressed in future PRP cases.

TARIFF ISSUES

Weather Normalization Adjustment

Atmos Kentucky proposed to update the period used to weather normalize revenues for the weather normalization adjustment (WNA) rider to the 20-year period ending March 2021. The WNA Rider is only used during the billing months of November-April 30. The Commission finds this update to be reasonable.

Performance Based Rate Mechanism

Atmos Kentucky proposed to remove the experimental designation from its Performance Based Rate Mechanism Tariff as the Commission had already approved the removal of the designation in Case No. 2015-00298.[254] As the Commission has already approved the revision, the Commission finds that the removal of the experimental designation from the Performance Based Rate Mechanism is reasonable and should be approved.

Tax Act Adjustment Factor

Atmos Kentucky proposed to establish a new Tax Act Adjustment Factor tariff to implement the effects of future changes of federal and state income taxes on the most recently approved base rates. The factor under the proposed tariff would be the

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[253] *See Matter of Missouri-American Water Company*, 637 S.W.3d at 127-8 (interpreting a statutory pipeline replacement mechanism that used similar language regarding the use of ADIT to calculate the revenue requirement and finding that it did not permit the imputation of NOL ADIT that did not exist).

[254] Case No. 2015-00298, *Request of Atmos Energy Corporation for Modification and Extension of its Gas Cost Adjustment Performance Based Ratemaking Mechanism* (Ky. PSC Mar. 31, 2016).

difference between the income tax expense included in the revenue requirement from Atmos Kentucky's most recent base rate proceeding and the calculated income tax expense if the change of the federal or state income tax rate had been in effect during the test year after applying the gross conversion factor.[255] The Attorney General recommended that the Commission reject the proposed rider as it is not necessary as the Commission already has the capability to address changes in the federal and state tax codes.[256] Atmos Kentucky argued that the proposed rider is not necessary because it is the only way to address future changes, but because it is the most efficient way.[257] Atmos Kentucky also argued that the Commission can still undertake its own analysis and require additional filings if the rider is approved and that it would save the Commission the need of conducting a proceeding in case of non-controversial tax changes.[258] As the Attorney General argued, there are already multiple processes in place at the Commission's and Atmos Kentucky's disposal to address changes in the federal and state tax codes. Therefore, the Commission finds that the proposed Tax Act Adjustment Factor Rider is unreasonable and should not be approved.

Parking Service.

Atmos Kentucky proposed to remove references to parking service from its tariff and that transportation accounts be fully cashed out for any remaining positive imbalance for the month. Atmos Kentucky claimed that its upstream pipelines do not currently offer

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[255] Direct Testimony of Brannon C. Taylor (Taylor Testimony), page 23, lines 14–18.

[256] Kollen Testimony, page 50, lines 8–15.

[257] Rebuttal Testimony of Joel J. Multer, page 12, lines 1–5.

[258] Rebuttal Testimony of Joel J. Multer, page 12, lines 10–19.

parking service[259] and that parking creates an opportunity for transportation customers and their marketers to attempt to engage in price arbitrage in times of rising natural gas prices by intentionally over nominating and over purchasing natural gas for that current month, knowing that 10 percent would be parked to the next month, thus avoiding purchasing natural gas that next month when prices are expected to be higher.[260] Atmos Kentucky indicated that with parking service removed, transportation customer behavior will change such that they will begin proactively resolving more of their daily and monthly imbalances and rely less on Atmos Kentucky's system balancing.[261] Atmos Kentucky claimed that there is no impact on its physical distribution system as a result of parked volumes as it ensures supply to its distribution system is balanced with customer requirements regardless of any volumes parked by transportation customers.[262] As there is no requirement that Atmos Kentucky provide parking service, the Commission finds that Atmos Kentucky's proposal to remove parking service references from its tariff and that transportation accounts be fully cashed out for any remaining positive imbalance for the month is reasonable and should be approved.

Natural Gas Weekly Pricing Index.

Atmos Kentucky proposed to replace references to the Natural Gas Weekly pricing index with the Gas Daily pricing index for imbalance pricing calculations, citing a substantial increase in the subscription price for Natural Gas Weekly and the publisher's

[259] Taylor Testimony, page 19, lines 8–9.

[260] Atmos Kentucky's response to Commission Staff's Second Request, Item 9(a)

[261] Atmos Kentucky's response to Commission Staff's Second Request, Item 9(d).

[262] Atmos Kentucky's response to Commission Staff's Second Request for Information, Item 8(c).

warnings of general copyright infringement concerns.[263] Atmos Kentucky already subscribes to Platt's Gas Daily publication and has the rights to utilize it in its calculations.[264] Atmos Kentucky also indicated that the change from using Natural Gas Weekly to using Gas Daily would have had no impact on the volumetric imbalance calculations for the past three calendar years and 2021 to date.[265] Atmos Kentucky also claimed that the proposal would have no direct impact on the Atmos Kentucky's Gas Cost Adjustment (GCA).[266] As the proposed revision would have had no impact on imbalance calculation and no direct impact to Atmos Kentucky's GCA, the Commission finds that Atmos Kentucky's proposal to replace references to the Natural Gas Weekly pricing index with the Gas Daily pricing index for imbalance pricing calculations is reasonable and should be approved.

Priorities of Curtailment

Atmos Kentucky proposed to revise the priorities of curtailment in its tariff. The current priorities require Atmos Kentucky to distinguish between certain customers based on their usage in mcf/day, which Atmos Kentucky claimed is a difficult standard to apply in real time in the event of a curtailment situation.[267] In addition, customers under the same rate schedule could be treated different under the current priorities.[268] Atmos Kentucky cited an example of two Rate G-1 customers, one burning 100 mcf/day and one

[263] Taylor Testimony, page 20, lines 9–10.

[264] Taylor Testimony, page 20, lines 16–19.

[265] Atmos Kentucky's response to Commission Staff's Second Request, Item 10(a).

[266] Atmos Kentucky's response to Commission Staff's Second Request, Item 10(c).

[267] Taylor Testimony, page 21, lines 4–6.

[268] Taylor Testimony, page 21, lines 11–13.

burning 49 mcf per day. Under the current curtailment priorities, the customer using 100 mcf/day would be instructed to go to zero before the smaller customer was affected.[269] Atmos Kentucky stated that the new curtailment priorities would operate strictly upon customer class so that customers served under the same class would not be treated differently.[270] The revisions would (1) combine all commercial service under Rate G-2 into Priority Level 2; (2) combine industrial service under Rates G-1 and T-4 to new Priority Level 3; (3) combine service under Rate G-2 and T-3, both interruptible, to new Priority Level 4; and (4) make flex sales transactions new Priority Level 5.[271] The Commission finds that the revisions to the curtailment priorities are reasonable and should be approved as customers under the same rate schedule should not be treated differently when it comes to curtailing service.

Operational Flow Orders.

Atmos Kentucky proposed to add language to its tariff regarding the ability to issue operational flow orders (OFO) to transportation customers and their marketers. The new provisions would require actions by Rate T-3 and T-4 customers to alleviate conditions that, in Atmos Kentucky's judgement, would jeopardize the operational integrity of Atmos Kentucky's system.[272] The proposal would also allow Atmos Kentucky to issue an OFO to an individual customer or marketer using transportation service without issuing an OFO to all transportation customers.[273] Atmos Kentucky explained that its current tariffs

[269] Taylor Testimony, page 21, lines 7–13.

[270] Taylor Testimony, page 21, lines 6–7.

[271] Taylor Testimony, page 15, lines 14–19.

[272] Taylor Testimony, page 16, lines 2–6.

[273] Taylor Testimony, page 22, lines 7–8.

contain a provision that authorizes curtailing transportation services when Atmos Kentucky is unable to confirm the customer's gas supply is actually being delivered to the system and that it has issued one such restriction over the last four calendar years.[274] Atmos Kentucky explained that it proposed the clarifying language to better describe the restriction as an Operational Flow Order, which is consistent with general pipeline practice and familiar to gas marketers.[275] Given the important purpose operational flow orders serve, the Commission finds that Atmos Kentucky's proposed revisions to its tariff regarding the ability to issue OFOs to transportation customers and their marketers is reasonable and should be approved.

Nonrecurring Charges.

In Case No. 2020-00141,[276] the Commission found that the calculation of nonrecurring charges should be revised because only the marginal costs related to the service should be recovered through special nonrecurring charges for service provided during normal working hours. In reaching that decision, the Commission found that personnel are paid for work during normal business hours regardless of whether they are on a field visit or not, and therefore labor costs included in nonrecurring charges that occur during regular business hours should be eliminated. By reflecting only the marginal cost of the service in nonrecurring charges, Atmos Kentucky's rates will be more in line with the principle of cost causation. Merely allocating a fixed expense of ordinary labor costs in special nonrecurring charges like reconnect and returned check charges creates

[274] Atmos Kentucky's response to Commission Staff's Second Request, Item 11(a).

[275] Atmos Kentucky's response to Commission Staff's Second Request, Item 11(b).

[276] Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020).

a mismatch between how Atmos Kentucky incurs expenses and how it recovers those expenses from customers. Instead of reflecting fixed costs in special nonrecurring charges that a utility incurs regardless of the number or timing of those nonrecurring services, including those fixed costs in rates for gas service more closely aligns those expenses with the actions that drive them. This approach to ratemaking is entirely consistent with the Commission's history of ensuring that rates reflect, to a reasonable degree, the principle of cost causation while simultaneously taking into account the health of the utility and the ability of the utility to provide the adequate, efficient and reasonable provision of service.

As demonstrated by the evidence of record, Atmos Kentucky relies on employee labor to perform its nonrecurring services.[277] Atmos Kentucky indicated that it would consider eliminating nonrecurring charges altogether and to recover the related revenue through base rates.[278] However, there are customer specific costs recovered through nonrecurring charges and the Commission believes that those costs are better recovered from the customers causing such costs. Based on the information above and using the cost support provided in this proceeding, the Commission finds that the following revisions should be made to Atmos Kentucky's nonrecurring charges.

	Current Charge	Revised Charge
Meter Set (Regular Hours)	$34.00	$3.00
Turn-On (Regular Hours)	23.00	3.00
Read (Regular Hours)	12.00	3.00
Reconnect Delinquent Service (Regular Hours)	39.00	3.00
Seasonal Charge (Regular Hours)	65.00	3.00

[277] Atmos Kentucky's response to Commission Staff's Third Request for Information (filed Sep. 16, 2021) (, Item 11(a).

[278] Atmos Kentucky's response to Commission Staff's Sixth Request for Information (filed Jan. 6, 2022), Item 3.

Returned Check Charge.

Atmos Kentucky charges a returned check charge of $25.00 when a payment is not honored by a customer's financial institution. As cost support for the charge, Atmos Kentucky initially provided a survey of returned check charges assessed by five banks that showed an average returned check charge of $35.60.[279] Atmos Kentucky later provided information indicating that it only deposited customer payments at one of the banks included in the survey.[280] Atmos Kentucky indicated that the other bank in which customer payments are deposited does not charge Atmos Kentucky for returned payments.[281] Finally, when asked to provide the amount Atmos Kentucky was charged by its banks for returned payments for calendar years 2016 through 2021, the information Atmos Kentucky provided showed that the average bank fee per returned payment was $3.30 for 2020 and 2021.[282] As a nonrecurring charge is only supposed to recover the costs of performing the service, the Commission finds that Atmos Kentucky's returned check charge should be reduced to $4.00.

Seasonal Charge.

Atmos Kentucky's cost justification for its after-hours seasonal charge indicated that the total cost to perform an after-hours seasonal reconnect was $59.97 while its

[279] Atmos Kentucky's response to Commission Staff's Third Request for Information (filed Sept. 16, 2021), Item 3, Attachment 1.

[280] Atmos Kentucky's response to Commission Staff's Fourth Request for Information (filed Nov. 24, 2021), Item 2.

[281] Atmos Kentucky's response to Commission Staff's Fifth Request for Information (filed Dec. 3, 2021), Item 4(a).

[282] Atmos Kentucky's response to Commission Staff's Seventh Request for Information (filed Feb. 2, 2022), Item 5.

tariffed rate for that service is $73.00.[283] In regards to the tariffed seasonal charge being more than the cost to perform the service, Atmos Kentucky argued that customers who terminate their service in early spring and reconnect in late fall avoid paying four to five months of the tariffed customer charge.[284] Atmos Kentucky also argued that the higher charge provided a level of deterrence to customers that drive costs through voluntary actions.[285]

Regarding nonrecurring charges, 807 KAR 5:006, Section 9(2) states "[a] charge shall relate directly to the service performed or action taken and shall yield only enough revenue to pay the expenses incurred in rendering the service." The regulation is clear that nonrecurring charges must be cost-based. There is nothing in the regulations allowing for a nonrecurring charge to exceed the expenses incurred in rendering the service in order to disincentivize customer conduct. Therefore, the Commission finds that Atmos Kentucky's after-hours seasonal charge should be reduced to $60 to only recover the cost of performing the service. No adjustment is necessary to nonrecurring charge revenue as a result of this change as there were no instances of this charge being assessed during the period used to forecast such revenues.

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[283] Atmos Kentucky's response to Commission Staff's Fifth Request for Information (filed Dec. 3, 2021), Item 3, Attachment 1, page 1 of 7.

[284] Atmos Kentucky's response to Commission Staff's Fourth Request for Information (filed Nov. 24, 2021), Item 1(d).

[285] Atmos Kentucky's response to Commission Staff's Fourth Request for Information (filed Nov. 24, 2021), Item 1(d).

Late Payment Charge.

Evidence collected in Case No. 2020-00085[286] challenged the efficiency of late payment charges to certain customers. Therefore, the Commission has recently reviewed utilities' late payment charges during rate cases. The information provided by Atmos Kentucky in Case No. 2020-00085 showed that the on-time pay percentage for residential customers actually increased while the late payment moratorium was in effect.[287]

Atmos Kentucky argued that its late payment charge is authorized under 807 KAR 5:006, Section 9(3)(h), that it is included in its tariff to encourage the customer to pay promptly, and that it is not based on an underlying cost.[288] Atmos Kentucky also indicated that it would consider eliminating late fees from its tariff altogether and recover the revenue through base rates.[289]

As the evidence indicates, the late payment charge does not appear to have the intended impact on residential customers' behavior. Given that, and the fact that Atmos Kentucky has suggested eliminating late payment fees altogether, the Commission finds that the residential late payment fee should be discontinued. Therefore, the Commission

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[286] Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19.*

[287] See No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19,* Atmos's response to Commission Staff's First Request for Information (filed Jul. 17, 2020), Item 9 and Atmos's response to Commission Staff's Second Request for Information (filed Jan. 14, 2021), Item 1.

[288] Atmos Kentucky's response to Commission Staff's Third Request for Information (filed Sept. 16, 2021), Item 11(b).

[289] Atmos Kentucky's response to Commission Staff's Sixth Request for Information (filed Jan. 6, 2022), Item 3.

reduces the test year late payment charge revenue by $0.874 million, which is the amount attributable to residential customers.

Temporary Turn-Off Charge.

Atmos Kentucky has been charging a fee when customers request that their gas service be turned off temporarily to accommodate temporary construction at their premises.[290] The amount of the charge is $20 for business hours and $25 for after normal business hours.[291] This charge has not been included in Atmos Kentucky's tariff. Atmos Kentucky indicated that if the Commission found that the charge should be included in the tariff, it would just stop charging customers for temporary off situations since they are infrequent and not causing a significant amount of costs.[292]

The Commission finds that this charge would meet the definition of a nonrecurring charge found in 807 KAR 5:006, Section 1(6), which defines a nonrecurring charge as:

> a charge or fee assessed to a customer to recover the specific cost of an activity, which:
> (a) Is due to a specific request for a certain type of service activity for which, once the activity is completed, additional charges are not incurred; and
> (b) Is limited to only recover the specific cost of the specific service.

Commission regulation 807 KAR 5:006, Section 9(2), requires nonrecurring charges to be included in a utility's tariff. Therefore, the Commission finds that if Atmos Kentucky is going to charge a temporary turn-off charge, it should be included in the tariff. However,

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[290] Atmos Kentucky's response to Commission Staff's Fifth Request for Information (filed Dec. 3, 2021), Item 1(a).

[291] Atmos Kentucky's response to Commission Staff's Fifth Request for Information (filed Dec. 3, 2021), Item 1(a).

[292] Atmos Kentucky's response to Commission Staff's Fifth Request for Information (filed Dec. 3, 2021), Item 1(b).

given that Atmos Kentucky has indicated that it will just stop charging the temporary turn-off charge if the Commission found it had to be included in the tariff, the Commission finds that Atmos Kentucky should stop charging the temporary turn-off charge.

KRS 278.160(2) states that "[n]o utility shall charge, demand, collect or receive from any person a greater or less compensation for any service rendered or to be rendered than that prescribed in its filed schedules, and no person shall receive any service from any utility for a compensation greater or less than that prescribed in such schedules." In addition, 807 KAR 5:006, Section 9(2), requires that any nonrecurring, customer specific charge must be included in the tariff. As Atmos Kentucky's tariff does not currently include the temporary turn-off charge, Atmos Kentucky appears to be in violation of KRS 278.160(2) and 807 KAR 5:006, Section 9(2). The Commission will open a separate proceeding to investigate Atmos Kentucky's alleged violation of KRS 278.160(2) and 807 KAR 5:006, Section 9(2).

IT IS THEREFORE ORDERED that:

1. The rates and charges proposed by Atmos Kentucky are denied.

2. The rates and charges as set forth in Appendix B to this Order are approved as fair, just and reasonable rates for Atmos Kentucky, and these rates and charges are approved for service on and after May 20, 2022.

3. Atmos Kentucky's proposal to remove the experimental designation from its Performance Based Rate Mechanism is approved.

4. Atmos Kentucky's proposed Tax Act Adjustment Factor Rider is denied.

5. Atmos Kentucky's proposal to remove parking service references from its tariff and that transportation accounts be fully cashed out for any remaining positive imbalance for the month is approved.

6. Atmos Kentucky's proposal to replace references to the Natural Gas Weekly pricing index with the Gas Daily pricing index for imbalance pricing calculations is approved.

7. Atmos Kentucky's proposal to revise its curtailment priorities is approved.

8. Atmos Kentucky's proposal to revise its tariff to allow it the ability to issues OFOs to transportation customers and their marketers is approved.

9. Atmos Kentucky's Meter Set Charge (Regular Hours) shall be reduced to $3.00.

10. Atmos Kentucky's Turn-On Charge (Regular Hours) shall be reduced to $3.00.

11. Atmos Kentucky's Read Charge (Regular Hours) shall be reduced to $3.00.

12. Atmos Kentucky's Reconnect Delinquent Service Charge (Regular Hours) shall be reduced to $3.00.

13. Atmos Kentucky's Seasonal Charge (Regular Hours) shall be reduced to $3.00.

14. Atmos Kentucky's Returned Check Charge shall be reduced to $4.00.

15. Atmos Kentucky's Seasonal Charge (After Hours) shall be reduced to $60.00.

16. Atmos Kentucky shall cease charging its residential late payment fee.

17. Atmos Kentucky shall cease charging its Temporary Turn-On Charge.

18. The Demand-Side Management (DSM) Lost Sales Adjustment component of Atmos Kentucky's DSM cost-recovery mechanism shall be reset to zero.

19. Within 20 days of the date of this Order, Atmos Kentucky shall file with the Commission, using the Commission's electronic Tariff Filing System, new tariff sheets setting forth the rates, charges, and modifications approved or as required herein and reflecting their effective date and that they were authorized by this Order.

20. This case is closed and removed from the Commission's docket.

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PUBLIC SERVICE COMMISSION

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Chairman

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Vice Chairman

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Commissioner

ENTERED

MAY 19 2022 bsb

KENTUCKY PUBLIC SERVICE COMMISSION

ATTEST:

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Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2021-00214 DATED MAY 19 2022

Atmos Energy Corporation - Kentucky Division
Case No. 2021-00214
Test Year Ended December 31, 2022
$ Millions

Atmos Requested Base Revenue Increase		
Atmos Requested Base Rate Increase	$	16.390
Atmos Revision in Calculated Base Revenue Deficiency		(1.338)
Atmos Revised Base Rate Revenue Deficiency	$	15.052
Rate Base Adjustments		
Include SSU Division 002 T-Lock Adjustment-Unrealized Gains Liability ADIT		(0.313)
Remove Other SSU Division 002 ADIT		(0.118)
Remove Accounts Payable - Construction		(0.501)
Remove Regulatory Asset for Rate Case Expenses		(0.035)
Reflect Effects from Amortization of Unprotected EDIT Over Three Years		0.166
Adjust CWC to Remove Non-Cash Items		(0.612)
Operating Income Adjustments		
Reduce Outside Services Expense Allocated from KY/Mid States Division		(0.405)
Amortize Unprotected EDIT Over Three Years Instead of Five Years		(3.460)
Amortize Remaining Rate Case Expense from Case 2018-00281 Over Three Years		(0.011)
Remove Social Organization/Service Club Dues		(0.164)
Reduce Misc. Service Revenues to Remove Labor from Charges		0.126
Reduce Misc. Service Revenues to Remove Residential Late Payment Fees		0.874
Reduce Misc. Service Revenues to Reduce Commercial and Public Authority Late Payment Fees		0.123
Rate of Return Adjustments		
Reflect Changes in Capital Structure		(2.041)
Adjust STD and LDT Rates		0.229
Reduce Return on Equity		(4.653)
Total Adjustments	$	(10.796)
Base Rate Increase before Amortization of Regulatory Liabilities	$	4.256
Less: Temporary Reduction Due to Amortization of COS and Depreciation Regulatory Liabilities	$	(1.644)
Net Increase in First Year	$	2.613

* Temporary reductions will continue until COS and depreciation reserve regulatory liabilities are fully amortized.

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2021-00214 DATED MAY 19 2022

The following rates and charges are prescribed for the customers served by Atmos Energy Corporation. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the authority of this Commission prior to the effective date of this Order.

RATE G-1
GENERAL FIRM SALES SERVICE

Base Charge

$19.30	per meter per month for residential service
$66.00	per meter per month for non-residential service

Distribution Charge

First	300	Mcf	$ 1.5483 per Mcf
Next	14, 700	Mcf	$ 1.0762 per Mcf
Over	15, 000	Mcf	$ 0.8888 per Mcf

RATE G-2
INTERRUPTIBLE SALES SERVICE

Base Charge

$520.00 per delivery point per month

Distribution Charge

First	15, 000	Mcf	$ 0.9557 per Mcf
Over	15, 000	Mcf	$ 0.7837 per Mcf

RATE T-3
INTERRUPTIBLE TRANSPORTATION SERVICE

Base Charge

$520.00 per delivery point per month

Distribution Charge for Interruptible Service

First	15, 000 Mcf	$ 0.9557 per Mcf
Over	15, 000 Mcf	$ 0.7837 per Mcf

RATE T-4
FIRM TRANSPORTATON SERVICE

Base Charge

$520.00 per delivery point per month

Distribution Charge for Firm Service

First	300 Mcf	$ 1.5483 per Mcf
Next	14, 700 Mcf	$ 1.0762 per Mcf
Over	15, 000 Mcf	$ 0.8888 per Mcf

Pipeline Replacement Program Rider Rates

	Monthly Customer Charge		Distribution Charge per Mcf
Rate G-1 (Residential)	$ 0.00		$0.0000
Rate G-1 (Non-Residential)	$ 0.00		$0.0000
Rate G-2	$ 0.00	1-15,000 Mcf	$0.0000
		Over 15,000 Mcf	$0.0000
Rate T-3	$ 0.00	1-15,000 Mcf	$0.0000
		Over 15,000 Mcf	$0.0000
Rate T-4	$ 0.00	1-300 Mcf	$0.0000
		301-15,000 Mcf	$0.0000
		Over 15,000 Mcf	$0.0000

Nonrecurring Charges

Meter Set (Regular Hours)	$3.00
Meter Set (After Hours)	$44.00
Turn-On (Regular Hours)	$3.00
Turn-On (After Hours)	$28.00
Read (Regular Hours)	$3.00
Read (After Hours)	$14.00
Reconnect Delinquent Service (Regular Hours)	$3.00
Reconnect Delinquent Service (After Hours)	$47.00
Seasonal Charge (Regular Hours)	$3.00
Seasonal Charge (After Hours)	$60.00
Meter Test Charge	$20.00
Returned Check Charge	$4.00
Late Payment Fee (G-1 Residential)	0%
Late Payment Fee (G-1 Commercial and Public Authority)	5%
Optional Facilities Charge for Electronic Flow Measurement Equipment	
Class 1 EFM equipment (<$7,500, including installation costs)	$75.00 per month
Class 2 EFM equipment (>$7,500, including installation costs)	$175.00 per month

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