

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF ATMOS)	CASE NO.
ENERGY CORPORATION FOR AN)	2024-00276
ADJUSTMENT OF RATES; APPROVAL OF)	
TARIFF REVISIONS; AND OTHER GENERAL)	
RELIEF)	

ORDER

On September 27, 2024, Atmos Energy Corporation (Atmos), tendered an application for a general rate adjustment, which was accepted for filing as of an October 11, 2024 Order granting a deviation from a provision of 807 KAR 5:001, Section 17(2)(b), notice requirements.¹ By Order dated October 17, 2024, the Commission, pursuant to KRS 278.190(2), suspended Atmos's proposed rates for six months through May 11, 2025. On May 8, 2025, Atmos filed notice that it would be placing its requested rates into effect effective May 12, 2025 subject to refund pursuant to KRS 278.190(2).

By Order dated October 3, 2024, the Attorney General of the Commonwealth of Kentucky, by and through the Office of Rate Intervention (Attorney General), was granted intervention. Atmos responded to four sets of requests for information submitted by

¹ Atmos's customer notice failed to accurately state the dollar amount change to average bills under the G-2 proposed rate. Atmos mailed a corrected notice to the six customers that take service under the G-2 (interruptible) rate and also printed revised notice in the applicable newspapers the week of October 6, 2024, outside the time permitted by 807 KAR 5:001, Section 17(2)(b).

Commission Staff and two sets submitted by the Attorney General.² The Attorney General submitted direct testimony on January 27, 2025, and responded to two sets of requests for information, one each from Atmos and Commission Staff.³ Atmos provided rebuttal testimony on March 10, 2025. A hearing was conducted May 6, 2025, through May 7, 2025. Atmos responded to two sets of post-hearing requests for information, one each from the Attorney General and Commission Staff.⁴

BACKGROUND

Atmos is a Texas corporation in good standing with its headquarters in Dallas, Texas, registered to do business in Kentucky and with its Kentucky office in Owensboro, Kentucky.⁵ Atmos is a utility that delivers natural gas to approximately 3.3 million ratepayers in eight states.⁶ Atmos 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

² Atmos's Response to Commission Staff's First Request for Information (Staff's First Request) (filed Oct. 25, 2024); Atmos's Response to Commission Staff's Second Request for Information (Staff's Second Request) (filed Dec. 2, 2024); Atmos's Response to Commission Staff's Third Request for Information (Staff's Third Request) (filed Jan. 3, 2025); Atmos's Response to Commission Staff's Fourth Request for Information (Staff's Fourth Request) (filed Apr. 18, 2025); Atmos's Response to Attorney General's First Request for Information (Attorney General's First Request) (filed Dec. 2, 2024); Atmos's Response to Attorney General's Second Request for Information (Attorney General's Second Request) (filed Jan. 3, 2025).

³ Attorney General's Response to Atmos's First Request for Information (Atmos's First Request) (filed Feb. 24, 2025); Attorney General's Response to Commission Staff's First Request for Information (Staff's First Request) (filed Feb. 24, 2025).

⁴ Atmos's Response to Commission Staff's Post-Hearing Request for Information (Staff's Post-Hearing Request) (filed May 28, 2025); Atmos's Response to Attorney General's Post-Hearing Request for Information (Attorney General's Post-Hearing Request) (filed May 28, 2025).

⁵ Application at 1, 3; Attachment FR_14(2)_Att1 and FR_14(2)_Att2.

⁶ Application at 1–2.

Division).⁷ Atmos's corporate offices in Dallas provide services to its operating divisions such as accounting, legal, human resources, rate administration, procurement, information technology, and customer service organizations. The costs of these centralized services are shared among the six regional Atmos operating divisions noted above, including the Kentucky/Mid-States division.⁸ As a result, Atmos allocates portions of the cost of company-wide centralized services and Kentucky/Mid-States division shared services to Kentucky operations for ratemaking purposes.⁹ Atmos's regulated gas distribution operation in Kentucky serves approximately 180,694 residential, commercial, and industrial customers in central and western Kentucky.¹⁰ Atmos last filed for a rate adjustment in Kentucky in Case No. 2021-00214.¹¹

Atmos asserted that the proposed rate adjustment is necessary to allow it to recover its reasonable operating costs and to earn a reasonable return on its investment while providing sufficient revenue to maintain its facilities and provide the level of service mandated by the Commission and Atmos customers.¹² Atmos requested an increase in revenue requirement used to calculate rates, increasing total revenue by \$33,001,164 using the forecasted test year rate base of \$628,233,491.¹³ Atmos projected its revenue

⁷ Application at 1–2.

⁸ Application at 1–2

⁹ Application at 11.

¹⁰ Application at 2.

¹¹ Case No. 2021-00214, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Final Order issued May 19, 2022).

¹² Application at 4.

¹³ Application at 5; Exhibit FR_16(7)(h)4_Att1.

requirement based on a forecasted test year ending on March 31, 2026, and using the year ending December 31, 2024, as a base period.¹⁴

The Attorney General's witnesses submitted several recommended adjustments to elements of Atmos's requested revenue requirement. In rebuttal testimony, Atmos agreed to certain reductions to revenue requirement recommended by the Attorney General including:¹⁵ (1) \$1.3 million as a result of an overstatement in employee benefits expense;¹⁶ (2) \$17,000 due to using an incorrect number of third-party vendor operations and maintenance (O&M) expense lag days in computing O&M expense;¹⁷ (3) \$526,000 resulting from updating composite allocation factors from the 12-month period ended September 30, 2023 to the 12-month period ended September 30, 2024;¹⁸ (4) \$85,000 reduced for a Net Operating Loss Carryforward Deferred Tax Assets (NOLC DTA) balance update provided during discovery;¹⁹ and (5) \$690,000 in NOLC DTA that excluded taxable income.²⁰ Atmos also agreed to a decrease in ad valorem taxes²¹ discussed below. The remaining ten Attorney General recommendations, totaling an

¹⁴ Application at 3.

¹⁵ All adjustments are grossed up to account for the accompanying reductions for income tax, Commission assessments, and bad debt.

¹⁶ Revised Direct Testimony of Randy A. Futral (filed April 24, 2025) (Futral Revised Direct Testimony) at 11; Rebuttal Testimony of Gregory K. Waller (Waller Rebuttal Testimony) at 11.

¹⁷ Revised Direct Testimony of Lane Kollen (filed Jan. 27, 2025) (Kollen Revised Direct Testimony) at 28; Rebuttal Testimony of Joe T. Christian (Christian Rebuttal Testimony) at 21.

¹⁸ Futral Revised Direct Testimony at 26. Waller Rebuttal Testimony at 23.

¹⁹ Kollen Revised Direct Testimony at 10-11; Waller Rebuttal Testimony at 5; Rebuttal Testimony of Joel J. Multer (Multer Rebuttal Testimony) at 2.

²⁰ Kollen Revised Direct Testimony at 14; Waller Rebuttal Testimony at 5.

²¹ Waller Rebuttal Testimony, Exhibit GKW-R-1 at 3.

additional \$16.109 million in revenue requirement reductions,²² are opposed by Atmos and are discussed below.

LEGAL STANDARD

The Commission's statutory obligation when reviewing a rate application is to determine whether the proposed rates are "fair, just and reasonable."²³ 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.²⁴ 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."²⁵ 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 proposed the 12 months ending March 31, 2026, as its forecasted test period to determine the reasonableness of its proposed rates. The Attorney General did

²² Futral Revised Direct Testimony at 17; Waller Rebuttal Testimony, Exhibit GKW-R-1 at 3.

²³ 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.").

²⁴ 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.").

²⁵ 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.").

not object to the proposed test period or suggest an alternative test period. The Commission finds Atmos Kentucky's forecasted test period to be within the provisions of KRS 278.192 and 807 KAR 5:001, Section 16(6), (7), and (8). Therefore, the Commission accepts the forecasted test period proposed by Atmos Kentucky for use in this proceeding.

VALUATION

Pursuant to KRS 278.290(1), the Commission is empowered to "ascertain and fix the value of the whole or any part of the property of any utility," and, in doing so, is given guidance by the legislature "in establishing value of utility property in connection with rates," and the Commission must "give due consideration" to a number of factors, including capital structure, original cost and "other elements of value recognized by law" in order to ascertain the value of any property under KRS 278.290 "for rate-making purposes." In its application, Atmos proposed to use the rate base method to calculate its revenue requirement and required increase.²⁶ The Commission has weighed the evidence filed in the case and finds that Atmos's base rates should be based on a 13-month average test period rate base of \$610,960,000.²⁷

DISCUSSION AND FINDINGS

Having reviewed the evidence and being sufficiently advised, the Commission has determined that certain adjustments to the rates proposed in Atmos's application are necessary. These adjustments are discussed in more detail below.

²⁶ Application, Attachment FR_16(6)(f)_Att1.

²⁷ Application, Attachment FR_16(6)(f)_Att1. Atmos's requested rate base is \$628,233,000, less the \$17,273,000 in revenue requirement reductions noted in Appendix A attached.

RATE BASE

Net Operating Loss Carryforward (NOLC) Accumulated Deferred Income Tax (ADIT)

Prior to its last rate case, Atmos tracked its deferred tax assets arising from net operating loss carryforward, referred to herein as NOLC ADIT, on a consolidated company basis for all of Atmos's divisions.²⁸ Atmos recorded that NOLC ADIT in Division 2, Account 190, and allocated a share of that NOLC ADIT to its Kentucky operations using a cost allocation percentage.²⁹ Atmos then included the NOLC ADIT allocated to it in rate base.

Including NOLC ADIT in rate base acts to increase rate base, and therefore, the amount of a utility's return. Federal tax law requires that certain NOLC ADIT arising from accelerated tax depreciation be included in rate base. The Internal Revenue Service (IRS) has indicated that including NOLC ADIT in rate base is intended to offset corresponding deferred tax liabilities arising from accelerated tax depreciation to reflect the extent to which the book-tax timing differences that gave rise to those deferred tax liabilities could not actually be used to defer tax expense.³⁰

In Atmos's last rate case, Case No. 2021-00214, the Commission noted that the inclusion of NOLC ADIT arising from losses in other jurisdictions in rate base would not serve the purpose given by the IRS for accounting for NOLC, because losses that are not attributable to this jurisdiction could not have arisen from the accelerated depreciation of utility property in this jurisdiction and any deferred tax liabilities associated with losses in

²⁸ Case No. 2021-00214, May 19, 2022 Order at 8.

²⁹ See Application, Schedule B, Tab B.5 B.

³⁰ See Private Letter Ruling 2015-34001, 2015 WL 4978111 (issued Aug. 21, 2015).

other jurisdictions is not offsetting rate base in Kentucky.³¹ The Commission also expressed concern about significant taxable losses in other Atmos divisions and that Atmos's percentage method of allocating NOLC ADIT to various divisions could result in those significant losses being unreasonably allocated to Atmos's Kentucky customers.³² Thus, the Commission found that:

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.³³

In the present case, Atmos used the NOLC ADIT balance allocated pursuant to the previous allocation methodology through September 30, 2021 as a starting point. Atmos then used "Pretax Book Income" and changes in ADIT balances for its Kentucky operations in Fiscal Years 2022 and 2023 and for Fiscal Year 2024 through June 30,

³¹ Case No. 2021-00214, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC Jun. 24, 2022), Order at 10.

³² Case No. 2021-00214, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 19, 2022), Order at 13–4; see also 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 15, explaining that there is an argument that including NOL ADIT attributable to losses in other jurisdictions would violate normalization rules in the same manner that using ADIT from other jurisdictions to offset Kentucky rate base would violate the normalization rules.

³³ Case No. 2021-00214, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 19, 2022), Order at 14.

2024 to calculate the utilization or generation of NOLC ADIT since September 30, 2021, which is the end of Atmos's Fiscal Year 2021. This resulted in approximately \$34,259,069 in NOLC ADIT being included in rate base as of the beginning of the forecasted period.³⁴

The Attorney General's witness, Lane Kollen, made three recommendations regarding the NOLC ADIT Atmos included in rate base. Atmos referred to those recommendations as NOLC DTA Adjustments 1 through 3,³⁵ which the Commission will use herein for ease of reference.

NOLC DTA Adjustment 1 was a recommendation to update the NOLC ADIT balance to reflect revenues from June 2024 through September 2024 based on updated information provided by Atmos for those periods, which resulted in a \$85,000 decrease in revenue requirement.³⁶ Atmos, which provided the updated information on which that adjustment was based, agreed to that proposed adjustment by the Attorney General.³⁷

NOLC DTA Adjustment 2 involves Atmos's compliance with the Commission's directive to apply only Kentucky losses to Kentucky operations as discussed above.³⁸ The Attorney General agreed that the NOLC ADIT balance should be calculated on a Kentucky-standalone basis, but argued that if doing so, it should be calculated on a standalone basis from the last time Atmos had no NOLC instead of using the previous balance from September 30, 2021, allocated on a percentage basis.³⁹ The Attorney

³⁴ See Application, Direct Testimony of Joel J. Multer (Multer Direct Testimony), Exhibit JJM-1.

³⁵ Kollen Revised Direct Testimony at 4–5.

³⁶ Kollen Revised Direct Testimony at 10–11.

³⁷ Waller Rebuttal Testimony at 5; Multer Rebuttal Testimony at 2.

³⁸ Kollen Revised Direct Testimony at 4–5.

³⁹ Kollen Revised Direct Testimony at 13.

General's witness stated that Atmos did not provide information for such a calculation and that the information regarding the utilization and generation of NOLC ADIT since the last rate case was insufficient.⁴⁰ Thus, the Attorney General's witness argued that unless the necessary information exists to calculate from the last time Atmos had no NOLC, that the Commission should allow Atmos to start with the previous percentage allocation methodology in this case alone, which he indicated results in a decrease in the NOLC ADIT in the amount of \$6.481 million and therefore a decrease in rate base in that amount and corresponding decrease of \$690,000 in revenue requirement.⁴¹

In rebuttal testimony, Atmos asserted that the Attorney General's testimony supporting use of the prior methodology to determine NOLC ADIT balance was results driven and that the Attorney General was only recommending that the Commission revert back to the percentage allocation method because it would achieve a lower NOLC ADIT in this case.⁴² Atmos responded to post-hearing data requests regarding historical NOLC ADIT information, indicating it had the data necessary to calculate the Kentucky-specific NOLC ADIT back to 2008, the last year Atmos did not have a NOLC balance.⁴³ However, Atmos did not review its records to separate Kentucky-specific losses from other jurisdictions' losses to determine this balance,⁴⁴ and Atmos agreed to the adjustment recommended by the Attorney General's witness.⁴⁵

⁴⁰ Kollen Revised Direct Testimony at 13–14.

⁴¹ Kollen Revised Direct Testimony at 14.

⁴² Multer Rebuttal Testimony at 5.

⁴³ Atmos's Response to Staff's Post-Hearing Request, Item 6(b).

⁴⁴ Atmos's Response to Staff's Post-Hearing Request, Item 6(c).

⁴⁵ Waller Rebuttal Testimony at 5.

NOLC DTA Adjustment 3 was the Attorney General's witness's argument that NOLC ADIT should only be included in rate base to the extent that it arises from differences between book depreciation and accelerated federal tax depreciation under Internal Revenue Code (IRC) normalization rules.⁴⁶ This reduction would result in a decrease in the NOLC ADIT of \$5.896 million and corresponding decrease of approximately \$627,000 in the revenue requirement.⁴⁷ Atmos objected to the Attorney General's recommendation that only NOLC ADIT associated with timing differences arising from accelerated tax depreciation should be reflected in rates because Atmos does not receive the economic benefit (in the form of cost-free capital) of deferring the income tax asset until the year it is applied to reduce taxes.⁴⁸ Atmos also claimed that the IRC only requires a minimum, not maximum amount of NOLC ADIT that must be included in rate base to avoid a normalization violation.⁴⁹ Although Atmos also took issue with the Attorney General's witness's calculation of the difference in book and accelerated depreciation, Atmos conceded that it chose not to incur the cost or effort required to provide this calculation.⁵⁰

The Attorney General's witness also recommended another reduction (NOLC DTA Adjustment 4) because Atmos did not include taxable income from the bridge period from October 1, 2024 through March 31, 2025,⁵¹ for which information was not available when

⁴⁶ Kollen Revised Direct Testimony at 14–15.

⁴⁷ Kollen Revised Direct Testimony at 19.

⁴⁸ Rebuttal Testimony of Joel J. Multer (Multer Rebuttal Testimony) at 9–10.

⁴⁹ Multer Rebuttal Testimony at 13.

⁵⁰ Multer Rebuttal Testimony at 18.

⁵¹ Kollen Revised Direct Testimony at 13.

earlier discovery requests were made. Atmos countered that the Attorney General assumed net positive income for this period.⁵² However, post-hearing discovery revealed net positive income of \$583,289 for that period, resulting in a decrease in Atmos's NOLC ADIT and a corresponding \$62,064 revenue requirement reduction.⁵³

Having reviewed the record and being otherwise sufficiently advised, the Commission makes the following findings with respect to the proposed adjustments to NOLC ADIT. The Commission finds that NOLC DTA Adjustment 1 is reasonable and should be accepted to reflect the most recent available information regarding the utilization and generation of NOLC ADIT, which would decrease the revenue requirement by \$85,000.

The Commission finds that NOLC DTA Adjustment 2 is reasonable and should be accepted, decreasing revenue requirement by approximately \$690,000. The Commission continues to believe that tracking the utilization and generation of NOLC ADIT on a Kentucky specific, standalone basis is more reasonable and appropriate than the percentage allocation method for the reasons discussed in Atmos's last rate case.⁵⁴ However, if the previous use of the percentage allocation method resulted in excess NOLC ADIT being allocated to Kentucky customers, the Commission is concerned that the excess may take an unreasonably long and unrealistic period to reverse using Atmos's new proposed method, which relies on net changes in ADIT, because the timing differences that generated the NOLC ADIT would be reversing in another jurisdiction. To

⁵² Multer Rebuttal Testimony at 19.

⁵³ Atmos's Response to Staff's Post-Hearing Request, Item 6(e).

⁵⁴ See Case No. 2021-00214, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 19, 2022), Order at 13-4.

avoid that issue and to more accurately reflect NOLC ADIT for Kentucky, the Commission generally believes that Kentucky-specific NOLC ADIT should be calculated from the last time Atmos had no carryforward if reliable information is available to make that calculation, but at minimum, that the percentage allocation should be checked against information that is available.

Atmos did not provide information in the record to allow for the calculation of NOLC ADIT from the last time it had no NOL carryforward.⁵⁵ However, although Atmos has the burden of supporting its revenue requirement, the Commission does not believe Atmos should be unduly punished here for not providing information that was not required by the Commission for its prior calculation of NOLC ADIT. Rather, the Commission finds that it would be more reasonable to stay with the percentage allocation for determining the historical NOLC ADIT prior to July 2024 until Atmos is able to provide additional information regarding the state specific accumulation of NOLC ADIT from the last time that Atmos had no NOLC. Thus, Atmos's decision to accept NOLC DTA Adjustment 2, which results in a revenue requirement decrease, is a reasonable compromise compared to removing all or significantly more NOLC ADIT from rate base.

Regarding NOLC DTA Adjustment 3, the Commission finds that the Attorney General's recommended adjustment should be denied. While the Attorney General is correct that only NOLC ADIT arising from accelerated tax depreciation is "protected"

⁵⁵ Atmos indicated at the hearing and in response to post-hearing requests for information that it had least some of the information necessary to make that calculation. However, it noted that there may be some questions about the veracity of that information or difficulties in determining what should and should not be included given the passage of time. Thus, if the information had been obtained at that point, there would have been no opportunity to test the methodology or the veracity of potentially questionable information. Hearing Testimony of Joel J. Multer, May 6, 2025, Hearing Video Transcript (HVT) at 15:28:53; Atmos's Response to Staff's Post-Hearing Request, Item 6(b).

pursuant to federal normalization rules, the inclusion of NOLC ADIT may still be considered reasonable for ratemaking purposes to reflect the extent to which corresponding deferred tax liabilities could not have been used to offset tax expense. Further, while Atmos did not perform the state specific calculations in this matter back to when it last had no NOLC ADIT and Atmos does bear the burden, the Commission does not believe Atmos should be unduly punished for not providing information that was not required by the Commission for prior calculations of NOLC ADIT without at least giving Atmos an additional opportunity to provide such information. Thus, under the circumstances, the Commission finds that it is reasonable to reject NOLC DTA Adjustment 3 and accept NOLC DTA Adjustment 2.

However, in doing so, the Commission finds that Atmos should continue to 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. Further, in Atmos's next application to increase base rates, Atmos Kentucky should file a report showing the generation and utilization of NOL ADIT for Kentucky since the last time that it had no NOL carryforwards. If Atmos Kentucky proposes to use a different method to reflect the generation and utilization of NOL ADIT for Kentucky in its revenue model, Atmos Kentucky should explain as part of the application, in detail, why using that method would be reasonable and why the Commission-ordered method is less reasonable or unavailable.

Finally, the Commission finds that NOLC DTA Adjustment 4 should be accepted, as post-hearing discovery revealed net positive income of \$583,289 for the bridge period from October 1, 2024 through March 31, 2025, resulting in a decrease in Atmos's NOLC ADIT and a corresponding \$62,064 revenue requirement reduction.

Vendor Supplied Portion of Construction Expenditures

Atmos temporarily finances its capital expenditures for plant and other assets as well as O&M expense, in part, through delayed payments to its vendors recorded as accounts payable. The Attorney General's witness, Kollen, recommended subtracting construction accounts payable from rate base because the delay between billing and payment of those accounts, at no cost, effectively provided Atmos with zero-cost financing.⁵⁶ Kollen noted that the Commission excluded those amounts from rate base in Atmos's last rate case for the same reason that the Commission removes amounts not financed by the utility from cash working capital.⁵⁷ Kollen further noted that Atmos neither appealed nor requested rehearing regarding that adjustment.⁵⁸ Kollen calculated that the adjustment amounts to a \$5.312 million reduction in base rates and a reduction in the base revenue increase of \$565,000.⁵⁹

Atmos alleged on rebuttal that the Attorney General's proposal improperly introduced a capital expenditures component into the calculation of the lead-lag study, which is intended to only look at expense items, and was therefore inconsistent with

⁵⁶ Kollen Revised Direct Testimony at 20–22.

⁵⁷ Kollen Revised Direct Testimony at 20–22.

⁵⁸ Kollen Revised Direct Testimony at 20-22; Case No. 2021-00214, (Ky. PSC May 19, 2022), Order at 17.

⁵⁹ Kollen Revised Direct Testimony at 22.

ratemaking principles associated with working capital.⁶⁰ Atmos also alleged that the Attorney General's analysis was incomplete because it proposed to use the 13-month average of construction accounts payable to reduce rate base but Atmos did not include construction work in progress (CWIP) as an element of rate base, and therefore, the adjustment would result in the removal of items that are not included in rate base.⁶¹

At the hearing, Atmos witness Christian testified that its rate base does not include CWIP, but that Atmos accrues Allowance for Funds Used During Construction (AFUDC). However, Mr. Christian was unclear in hearing testimony regarding exactly how Atmos's AFUDC calculation is completed, and therefore, how the lag between receipt and payment of invoicing for amounts in construction accounts payable is handled. Mr. Christian did indicate that the company uses the methodology approved by Federal Energy Regulatory Commission (FERC) regulations.⁶²

The Commission finds that the Attorney General's recommendation should be denied. The Commission has generally found that a utility may account for construction carrying costs by either including CWIP in rate base or by capitalizing AFUDC.⁶³ In general, including CWIP in rate base accounts for construction carrying costs by allowing a utility to recover a return, usually at the utility's weighted average cost of capital (WACC), on the utility's CWIP balance during the test period. Conversely, in Kentucky,

⁶⁰ Christian Rebuttal Testimony at 17.

⁶¹ Christian Rebuttal Testimony at 17.

⁶² Hearing Testimony of Joe T. Christian, May 6, 2025, HVT at 17:30:52; Multer Rebuttal Testimony at 17.

⁶³ See Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 7, 2019), Order at 25, noting that a utility may use AFUDC or CWIP and that Atmos uses CWIP; see also 18 C.F.R. § 35.25(e)-(f).

a utility that uses AFUDC will not generally include any CWIP in rate base but will track the carrying costs on CWIP on an ongoing basis and will then capitalize these costs for future recovery.⁶⁴

Although the Commission agrees with the Attorney General's witness that sources of cost-free capital generally should reduce rate base,⁶⁵ in the present case, no corresponding CWIP is included in rate base to offset—meaning the cost that is being funded at no cost due to the lag between billing and payment is not included in rate base so there is nothing to offset. Further, while some adjustment would likely be necessary if Atmos provided evidence that it was accruing AFUDC on construction accounts payable before payment was made on those invoices, the adjustment would be different (and potentially larger or smaller) than simply removing construction accounts payable from rate base. However, no evidence has been presented in this matter that Atmos accrues AFUDC on construction accounts payable before the payment of the invoices by Atmos. Thus, while the Commission accepted this adjustment in Atmos's last rate case, the facts in this case do not support finding that Atmos's revenue requirement includes carrying costs on construction accounts payable, and therefore, the Commission finds that this adjustment proposed by the Attorney General should be denied in this case.⁶⁶

Cash Working Capital (CWC)

⁶⁴ See Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 7, 2019) (discussing CWIP and AFUDC); *but see* 18 C.F.R. § 35.25(e)-(f).

⁶⁵ See Case No. 2021-00214, May 19, 2022 Order at 16–17.

⁶⁶ If the evidence in a future case indicates that Atmos's cost of service includes carrying costs on the amounts in question, then the Commission may reach a different conclusion.

Atmos filed a lead-lag study to calculate the extent to which CWC should be included in rate base. However, Atmos included non-cash depreciation expense, non-cash deferred income tax expense, and the non-cash growth component of the return on equity (ROE) in its CWC calculations.⁶⁷

The Attorney General's witness, Kollen, noted that Atmos included the non-cash expenses using 34.63 revenue lag days offset by zero expense lag days for each of the non-cash expenses, which resulted in an increase of \$9.817 million in the CWC added to rate base, all else equal.⁶⁸ Witness Kollen asserted that the purpose of CWC calculations is to quantify the cash investment provided by either investors (positive) or customers (negative) on average for the delay in cash revenues to recover cash expenses incurred over the course of the test year, but stated that there will never be a cash disbursement for depreciation expense. Witness Kollen also indicated that Atmos is able to retain the carrying charge value of this non-cash expense in the calculation of rate base and between rate cases, because the net accumulated depreciation and accumulated deferred income taxes are subtracted from rate base on a lagged basis.⁶⁹ Thus, the Attorney General recommended excluding all non-cash expenses from the CWC calculations, reducing the CWC included in rate base by \$9.817 million and the base revenue requirement by \$1.045 million.⁷⁰ Atmos disagreed with this recommendation in rebuttal and argued that the inclusion of these items in the study and assigning a zero

⁶⁷ Kollen Revised Direct testimony at 22.

⁶⁸ Kollen Revised Direct testimony at 22.

⁶⁹ Kollen Revised Direct testimony at 22.

⁷⁰ Kollen Revised Direct testimony at 26.

payment lag recognizes that the investor funding has occurred, but that it has not been recovered from the customer.⁷¹

This issue was considered in Commission Case No. 2021-00214, where the Commission found that “[n]oncash expenses are not appropriate to include in the CWC determination.”⁷² Similarly, here the Commission finds that non-cash items should be removed from the lead-lag study. The Commission continues to agree that non-cash expenses should not be included in the lead-lag study when calculating CWC, because working capital is not necessary to fund those expenses. Further, even if it were necessary, an expense lag of zero days would not be appropriate here given delays in how the non-cash items are reflected in rate base. Thus, the Commission finds that the Attorney General’s proposed adjustment should be accepted as reasonable, and that CWC should be reduced by \$9.817 million and that the revenue requirement for base rates should be reduced by \$1.045 million.

OPERATING INCOME ADJUSTMENTS

Payroll Expense and Related Payroll Taxes

The Attorney General’s witness, Randy Futral, recommended reducing Atmos’s payroll expense and related payroll tax expense to account for differences in the historical payroll increases and the projected increase between the base period and the forecasted period. Witness Futral argued that the projected labor expense increase between 2024 and the test year was unduly high given the two pay increases likely to occur during that period, because it assumes full employment during that period, which the Attorney

⁷¹ Christian Rebuttal Testimony at 18.

⁷² Case No. 2021-00214, (Ky. PSC May 19, 2022), Order at 20.

General indicated was inconsistent with past years.⁷³ Witness Futral proposed to adjust the 2024 amounts to reflect projected 3.5 percent raises, but indicated that the Commission should account for vacancies from full employment. Accordingly, witness Futral proposed to reduce the test year payroll and payroll tax expense by \$1.044 million for a grossed-up test year reduction of \$1.056 million.⁷⁴

In rebuttal testimony, Atmos acknowledged that it assumed full employment in its projections, despite typically having some turnover in historical periods, but argued that the Attorney General's use of Fiscal Year 2024 wage information, adjusted for expected raises, failed to account for other labor related variances that occurred in Fiscal Year 2024 that are not expected to be repeated in Fiscal Year 2025—(1) a capitalization rate of 59.7 percent in Fiscal Year 2024 as compared to 56.9 percent projected for Fiscal Year 2025; and (2) nine projected new positions, including seven new line location technicians and two compliance technicians.⁷⁵ Atmos asserted that when those variances are accounted for that projected expense would exceed the amount it included in base rates.

Atmos's rebuttal testimony also indicated that it used a capitalization for the test period labor expense that was higher than its historical capitalization rate.⁷⁶ Further, while Atmos argued that using the capitalization rate for its budget forecast was more accurate than using the 2024 capitalization rate, as effectively used by the Attorney General, the evidence indicated that its budgeted rates have been historically above its actual

⁷³ Futral Revised Direct Testimony at 7–8.

⁷⁴ Futral Revised Direct Testimony at 10–11.

⁷⁵ Waller Rebuttal Testimony at 9. Atmos stated that the new positions were created to enhance damage prevention and to bring line locating in house. Atmos reduced contracted line locating expense in the 2025 budget by \$600,000 that offset the cost of the new line locating positions.

⁷⁶ Waller Rebuttal Testimony at 8.

capitalization rates.⁷⁷ The Attorney General proposed a decrease in payroll expense based on the actual Fiscal Year 2024 capitalization rate compared to the budgeted rate used by Atmos in its original filing; Atmos's witness Waller indicated that using the Fiscal Year 2024 capitalization rate for payroll and related expenses would result in a \$538,225 reduction in revenue requirement.⁷⁸

The Commission finds that the Attorney General's recommended payroll expense adjustment should be rejected, in part, and accepted, in part. The Commission has not generally made adjustments due to vacancies where evidence showed that the utility intended to fill the positions,⁷⁹ and therefore, finds that an adjustment based solely on vacant positions would not be appropriate in this case, given that Atmos provided evidence that the positions have or will be filled. However, the Commission finds that an adjustment should be made to Atmos's revenue requirement to reflect a higher capitalization rate than that used by Atmos in the forecasted period. Specifically, the Commission finds that the extent to which Atmos's payroll expense is included in O&M expense should be based on Atmos's actual FY 2024 capitalization rate of 59.7 percent as opposed to the forecasted FY 2025 capitalization rate of 56.9 percent. The FY 2024 capitalization rate is reasonable, because the FY 2025 capitalization rate is lower than forecasted rates in previous years, previous years forecasted rates have been lower than

⁷⁷ Attorney General's Post-Hearing Brief (Attorney General's Brief) at 13-14; Atmos's Responses to Staff's Post Hearing Request for Information, Item 5 (indicating actual capitalization rates were higher than budgeted and were in line with the Fiscal Year 2024 rate used by the Attorney General in its payroll adjustment).

⁷⁸ Attorney General's Brief at 13-14; Waller Rebuttal Testimony at 8.

⁷⁹ Case No. 2023-00191, *Electronic Application of Kentucky-American Water Company for an Adjustment of Rates, a Certificate of Public Convenience and Necessity for Installation of Advanced Metering Infrastructure, Approval of Regulatory and Accounting Treatments, and Tariff Revisions* (Ky. PSC May 3, 2024), Order at 10.

actual rates, and the actual capitalization rate for FY 2024 is in line with rates in other historical years.⁸⁰ Thus, the Commission finds that a \$538,225 reduction in revenue requirement should be applied to reflect the effect on payroll expense of that capitalization rate adjustment.

Ad Valorem Tax

The Attorney General recommended a reduction of \$3.216 million in ad valorem tax expenses from the \$12.385 million Atmos projection calculated in the table below.⁸¹ The Attorney General asserted that all components of the Atmos's projection were based on estimates used to record its accounting accruals and in its projection of gross plant balances and that no part of the application calculation was based on actual ad valorem taxes paid or actual gross or net plant balances. The Attorney General's reduction calculation was based on monthly accruals of \$792,000 each month starting in October 2024 less the \$340,000 that is recovered via the Pipeline Replacement Program (PRP) Rider.⁸²

⁸⁰ In Atmos's Response to Staff's Post-Hearing Request, Item 5, Atmos provided the following budgeted and actual capitalization rates for FY 2020 through FY 2023:

Fiscal Year	Budgeted	Actual
2020	57.6%	60.1%
2021	57.6%	60.7%
2022	57.4%	60.2%
2023	57.9%	58.7%

⁸¹ Waller Rebuttal Testimony at 9-10.

⁸² Futral Revised Direct Testimony at 17.

Division 009 Only

Base Period Ad Valorem - Accrual	\$ 11,322,473
Remove non-recurring adjustment	1,000,000
Ad Valorem Recovered in PRP Rates Case No. 2023-00231	(339,931)
Adjusted Base Period Ad Valorem	<u>\$ 11,982,542</u>
Ending Base Period Gross Plant	\$ 909,763,471
Ad Valorem Rate	1.32%
Ending Forecasted Period Gross Plant	\$ 940,325,173
Forecasted Period Ad Valorem - Accrual	\$ 12,385,072

In rebuttal, Atmos rejected the Attorney General's proposed adjustment, stating that Atmos had now received its total tax bill for 2024 from the Kentucky Department of Revenue of \$1,075,778 and used this to calculate a new adjustment.⁸³ Using the \$1,075,778 amount, Atmos estimated its total ad valorem tax expense of \$9,424,575 using the table below.

⁸³ Waller Rebuttal Testimony at 12–13.

Table GKW-R-3 Estimated 2024 Kentucky State and Local Taxes			
Property Class	Tax Rate Per \$100	Noticed Value	State Tax Due
Real Estate	0.109 \$	647,451,382 \$	705,722
Tangible Property	0.45	79,415,375	357,369
Business Inventory	0.05	25,373,751	12,687
Total State Taxes	\$	752,240,508	\$ 1,075,778
Local Taxes	Noticed Value	Tax Rate Per \$100	Est. Local Taxes
	\$ 752,240,508	1.109857369	\$ 8,348,797
Total Est State & Local Taxes			\$ 9,424,575

Atmos then subtracted \$339,931 to recognize the amount of ad valorem recovered in its PRP. Then, Atmos calculated an effective expense ratio and applied that ratio to the plant forecast for the test period. The result is \$9,389,824.⁸⁴ Atmos also asserted that the Attorney General ignored that plant investment is forecasted to grow over the course of the test period. Atmos included an additional \$500,000 increase in Ad Valorem expense to account for a previously anticipated change in Kentucky Department of Revenue methodology that was expected to take place on January 1, 2026. This resulted in a test-period \$9,889,824 in ad valorem expense.⁸⁵ Atmos stated that given the uncertainty of the methodology change that the additional \$500,000 increase would be removed should the Commission approve the Tax Rider Tariff.⁸⁶

⁸⁴ Waller Rebuttal Testimony at 13.

⁸⁵ Waller Rebuttal Testimony at 14.

⁸⁶ Waller Rebuttal Testimony at 15.

The Commission finds that a \$3.03 million⁸⁷ reduction to revenue requirement should be applied to align the estimated ad valorem expense as originally filed with subsequent actual tax bills for 2024. This reduction includes elimination of the \$500,000 revenue requirement increase previously included by Atmos due to the potential January 1, 2026 tax change. Atmos indicated at hearing that it no longer anticipated that this tax change would take effect.⁸⁸

Corporate Expenses

The Attorney General challenged the full inclusion of Atmos's expenses allocated to Kentucky for Director and Officers' insurance, Board of Directors compensation,⁸⁹ and investor relations expenses, suggesting that Atmos's shareholders should bear 50 percent of these expenses, arguing that the majority of the benefits arising from these expenses are retained by shareholders.⁹⁰ This would result in a \$65,000 revenue reduction for insurance expense and \$19,000 for investor relations.⁹¹

Atmos responded that these expenses are prudent and necessary for providing service and their inclusion is supported by Commission precedent, which held that these expenses reduce costs that would be passed on to ratepayers.⁹²

⁸⁷ See Attorney General's Brief at 17.

⁸⁸ Hearing Testimony of Gregory K. Waller, May 6, 2025, HVT at 13:20:30.

⁸⁹ Less Board of Directors retirement expenses. See Futral Revised Direct Testimony at 19, footnote 20.

⁹⁰ Futral Revised Direct Testimony at 19–20.

⁹¹ Futral Revised Direct Testimony at 20. The Attorney General testimony omits a reduction for Board of Directors compensation.

⁹² Waller Rebuttal Testimony at 15-16; Case No. 2024-00092, *Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; and Other Relief* (Ky. PSC Dec. 30, 2024), Order at 24.

The Commission finds that none of the referenced corporate expenses should be eliminated from recovery by Atmos. Costs from litigation against executives would be passed on, at least in part, to ratepayers. Investor relations expense is a necessary component of raising necessary capital for the company. Although shareholders also benefit from these expenses, attracting and maintaining investors is also a key element for financial stability, which benefits ratepayers as well. The Attorney General has not offered a compelling basis for what percentage of these expenses should be excluded from recovery. Attorney General witness Futral indicated that the recommended 50/50 split was approved by the Florida Public Service Commission but did not identify any factual or logical bases for selection of this split.⁹³

Dues

The Attorney General recommended eliminating recovery of American Gas Association (AGA) and Kentucky Chamber of Commerce dues, resulting in a grossed-up revenue requirement adjustment of \$78,000.⁹⁴ The Commission previously disallowed recovery of these dues on the basis that Atmos did not establish that these dues did not include prohibited lobbying costs.⁹⁵ Atmos argued that AGA dues should be recoverable, because among other things, AGA exists to fulfill the needs of the local natural gas distribution companies and thereby improve the industry's ability to better serve its customers. Atmos similarly notes that Chambers of Commerce are the primary organizations within a community to coordinate efforts to strengthen the economy and

⁹³ Hearing Testimony of Randy A. Futral, May 7, 2025, HVT at 10:04:38.

⁹⁴ Futral Revised Direct Testimony at 22.

⁹⁵ Case No. 2021-00214, (Ky. PSC May 19, 2022), Order at 24–25.

employment opportunities, and thereby, supports natural gas load growth in the area. Atmos also argued that engagement with these organizations allows them to promote safe practices.⁹⁶ Atmos also stated that it removed lobbying costs associated with these entities by reducing the recovery based on the percentage of cost attributable to lobbying as indicated on the dues invoices.⁹⁷

The Commission finds that dues expenses should be excluded from recovery. Without knowing how the AGA or Chambers of Commerce determine the percentage of dues attributable to lobbying noted on their invoices, the Commission cannot find that these percentages are based on actual lobbying spending. Furthermore, Atmos has not established that these expenses benefit ratepayers.

RATE OF RETURN

Return on Equity (ROE)

In its application, Atmos Energy Corporation (Atmos) used multiple models to develop its ROE recommendation, including the Discounted Cash Flow (DCF) model, the Capital Asset Pricing Model (CAPM), and the Risk Premium Model (RPM) (collectively, Models).⁹⁸ In its analysis, Atmos used a utility proxy group comprised of six natural gas utilities (Utility Proxy Group) and a general proxy group comprised of 53 domestic, non-price regulated companies (Non-Price Regulated Proxy Group).⁹⁹ The proxy groups were selected on the basis of several risk measures, including both business risk and financial

⁹⁶ Waller Rebuttal Testimony at 20-21.

⁹⁷ Hearing Testimony of Gregory K. Waller, May 6, 2025, HVT at 14:35:52.

⁹⁸ Direct Testimony of Dylan D'Ascendis (D'Ascendis Direct Testimony) at 3.

⁹⁹ D'Ascendis Direct Testimony at 3-4.

risk, as well as a set of criteria to develop proxy groups which were proffered as highly representative of the risks and prospects faced by Atmos.¹⁰⁰ Additionally, Atmos relied upon the Predictive Risk Premium Model (PRPM) in its estimation of the equity risk premium used in its PRM and CAPM analyses.¹⁰¹ Atmos's estimated ROE results from the Models ranged from 9.93 percent to 12.05 percent, which were then adjusted based on company-specific risk factors.¹⁰² The adjustments applied to the common equity cost rates included a size adjustment, credit risk adjustment, and a flotation cost adjustment.¹⁰³ After these adjustments, the ROE estimates ranged from 10.12 percent to 12.12 percent, and Atmos recommended an ROE of 10.95 percent.¹⁰⁴ No adjustment to the ROE based on Atmos's PRP rider was proposed.¹⁰⁵ The estimated ROE results and adjustments are shown in the table below.¹⁰⁶

¹⁰⁰ Atmos's Response to Staff's Second Request for Information (Staff's Second Request), Item 10.

¹⁰¹ D'Ascendis Direct Testimony at 29.

¹⁰² D'Ascendis Direct Testimony at 4–5.

¹⁰³ D'Ascendis Direct Testimony at 4.

¹⁰⁴ D'Ascendis Direct Testimony at 5.

¹⁰⁵ D'Ascendis Direct Testimony at 62.

¹⁰⁶ D'Ascendis Direct Testimony, Table 2 at 4.

Discounted Cash Flow Model	9.93%
Risk Premium Model	10.80%
Capital Asset Pricing Model	11.36%
Market Models Applied to Comparable Risk, Non-Price Regulated Companies	12.05%
Indicated Range of Common Equity Cost Rates Before Adjustments for Company-Specific Risk	9.93% - 12.05%
Size Adjustment	0.05%
Credit Risk Adjustment	-0.04%
Flotation Cost Adjustment	0.06%
Indicated Range of Common Equity Cost Rates after Adjustment	10.12% - 12.12%
Recommended Cost of Common Equity	10.95%

The Attorney General provided alternative ROE estimates using the CAPM and the DCF model applied to one proxy group consisting of seven natural gas distribution companies.¹⁰⁷ In regard to the CAPM analysis, the Attorney General argued that because a considerable amount of judgment must be employed in determining the market return and the expected risk premium elements of the CAPM equation, it was less accurate than the DCF model.¹⁰⁸ However, the Attorney General relied on both the CAPM and DCF models in determining Atmos's ROE.¹⁰⁹ Consistent with the midpoint between the average and median growth rate DCF ROE estimates and the range of the CAPM

¹⁰⁷ Direct Testimony of Richard Baudino (Baudino Direct Testimony) at 2–3.

¹⁰⁸ Baudino Direct Testimony at 24.

¹⁰⁹ Baudino Direct Testimony at 3.

estimates, the Attorney General recommended an ROE of 9.40 percent for Atmos.¹¹⁰ Additionally, the Attorney General recommended a 9.30 percent ROE be applied to investments collected through the PRP.¹¹¹ The following table summarizes Attorney General witness Richard A. Baudino's results:¹¹²

Summary of ROE Estimates	
<u>DCF Methodology</u>	
Average Growth Rates	
- High	9.75%
- Low	8.25%
- Average	9.33%
Median Growth Rates	
- High	10.14%
- Low	8.11%
- Average	9.46%
<u>CAPM Methodology</u>	
Forward-looking Market Return:	9.71%
Historical Risk Premium:	
- Arithmetic Mean	10.52%
- Supply Side MRP	9.73%
- Supply Side Less WWI Bias	8.92%
Kroll MRP	8.72%
KMPG MRP	8.72%
IESE MRP Survey	9.14%
Damodaran MRP	8.30%

The Attorney General argued that this recommendation fully reflected current economic and financial market conditions at the time the testimony was prepared, and that it provides a fair return to investors on a low-risk regulated gas distribution utility

¹¹⁰ Direct Testimony of Richard A. Baudino (Baudino Direct Testimony) at 33.

¹¹¹ Baudino Direct Testimony at 37.

¹¹² Baudino Direct Testimony, Table 1 at 33.

investment such as Atmos.¹¹³ The Attorney General argued that Atmos's recommended ROE of 10.95 percent was grossly excessive and should be rejected.¹¹⁴ In addition, Attorney General witness Baudino argued that Atmos's ROE recommendation was a clear and obvious outlier when compared to recent commission-approved ROEs.¹¹⁵ In regard to Atmos's DCF calculation, although Atmos relied on earnings growth forecasts generated by Value Line Investment Survey (Value Line), witness Baudino argued that Atmos should have considered Value Line's dividend growth forecasts as well. While Baudino agreed that security analysts' earnings growth forecasts have a more significant influence on market prices than dividend growth expectations, he also asserted that forecasted dividend growth should also be considered because dividend payments are such a significant portion of the total return to utility shareholders.¹¹⁶ The Attorney General noted that his DCF results were lower than Atmos's results, and stated that this was primarily due to the use of updated stock prices and growth rates, as well as Value Line's projected dividend growth rates.¹¹⁷ The Attorney General's position was that by not including dividend forecasted growth rates, Atmos's DCF analysis was limited and results were overstated.¹¹⁸ Regarding the RPM analyses, the Attorney General argued that the analyses were too imprecise and should only be used as a guide for estimating

¹¹³ Baudino Direct Testimony at 3.

¹¹⁴ Baudino Direct Testimony at 38.

¹¹⁵ Baudino Direct Testimony at 39.

¹¹⁶ Baudino Direct Testimony at 40.

¹¹⁷ Baudino Direct Testimony at 40.

¹¹⁸ Baudino Direct Testimony at 40.

ROE in regulated utility proceedings.¹¹⁹ The Attorney General argued that the RPM ROE results were outliers, and did not represent current investor required ROE for regulated gas utilities.¹²⁰ In addition, the Attorney General argued that the Atmos's PRPM should be rejected because it is unproven, produced excessive ROE results and not widely accepted noting that it had been rejected by the Florida Public Service Commission.¹²¹ The Attorney General argued that Atmos's CAPM and ECAPM results were based on excessive earnings growth rates and market returns, and are so overstated for regulated gas utilities that they should be rejected out of hand.¹²² The use of ECAPM to correct the CAPM results for companies with betas less than 1.0 is another indication that the model is not sufficiently accurate.¹²³ Finally, the Attorney General argued that Atmos's use of unregulated companies as proxies for a regulated company, and the inclusion of size adjustments and flotation cost adjustments, are inappropriate and should be rejected.¹²⁴

In rebuttal, Atmos provided an updated ROE analysis using the same methods and updated data as of January 31, 2025.¹²⁵ Additionally, Atmos updated its Utility Proxy Group to include Southwest Gas Holdings, Inc (SWX), and to no longer include Yahoo! Finance projected five-year earnings per share growth rates in the DCF calculations, as

¹¹⁹ Baudino Direct Testimony at 40–41.

¹²⁰ Baudino Direct Testimony at 49.

¹²¹ Baudino Direct Testimony at 45–48.

¹²² Baudino Direct Testimony at 52–54.

¹²³ Baudino Direct Testimony at 55.

¹²⁴ Baudino Direct Testimony at 56–60.

¹²⁵ Rebuttal Testimony of Dylan D'Ascendis (D'Ascendis Rebuttal Testimony) at 1.

they were no longer available.¹²⁶ This updated analysis resulted in estimated ROEs ranging from 10.43 percent to 11.91 percent with adjustments and 10.37 percent to 11.85 percent without.¹²⁷ From these ranges, Atmos maintained its ROE recommendation of 10.95 percent.¹²⁸

Atmos disagreed with several aspects of the Attorney General's analysis, and argued that the ROE recommendation was significantly understated.¹²⁹ Concerning the DCF analysis, Atmos disagreed with the inclusion of dividend per share growth rates, arguing that the use of earnings per share growth rates is more appropriate in DCF analyses.¹³⁰ Atmos also found fault with the Attorney General's CAPM analysis, specifically the recency of the data used, the approaches used in calculating the market risk premium, and failure to incorporate the empirical CAPM analysis to correct for low-beta values.¹³¹

In its brief, Atmos maintained the appropriateness of a 10.95 percent ROE, and argued that it is commensurate with returns in business with similar risk.¹³² Atmos further maintained that the use of multiple models added reliability to the estimated ROE.¹³³ Regarding the authorized ROE for PRP, Atmos argued that the lower risk of having a

¹²⁶ D'Ascendis Rebuttal Testimony at 3.

¹²⁷ D'Ascendis Rebuttal Testimony at 1–2.

¹²⁸ D'Ascendis Rebuttal Testimony at 4.

¹²⁹ D'Ascendis Rebuttal Testimony at 16.

¹³⁰ D'Ascendis Rebuttal Testimony at 19–20.

¹³¹ D'Ascendis Rebuttal Testimony at 26–27.

¹³² Atmos's Post-Hearing Brief (Atmos Brief) at 33.

¹³³ Atmos Brief at 33.

PRP, if any, would already be subsumed in the market data for its Utility Proxy Group.¹³⁴ Atmos maintained that its ROE should not be adjusted due to its PRP Rider.¹³⁵

The Attorney General's brief reiterated the ROE recommendation of 9.4 percent, based on the results of the DCF model and CAPM model using both historical and forecasted data from multiple sources.¹³⁶ The models were applied to a proxy group of the same seven gas distribution companies utilized by Atmos, with one additional company.¹³⁷ The Attorney General noted the controversy over the use of the CAPM model and historical MRP calculated over long periods, and the additional sources used to supplement his analyses to mitigate the risk of upward bias.¹³⁸ The Attorney General reiterated his recommended 9.3 percent ROE for the PRP.¹³⁹ The Attorney General argued that Atmos's ROE results were grossly excessive and unreasonable.¹⁴⁰ Additionally, the Attorney General took issue with assumptions and calculations in Atmos's DCF, CAPM, and RPM analyses, as well as the use of both the CAPM and PRPM models in its analyses.¹⁴¹ Finally, the Attorney General argued against the use of a non-regulated proxy group, size adjustments, and flotation cost adjustments.¹⁴²

¹³⁴ Atmos Brief at 33.

¹³⁵ Atmos Brief at 34.

¹³⁶ Attorney General's Brief at 22.

¹³⁷ Attorney General Brief at 22. The Commission notes that the Attorney General included Southwest Gas Holdings, Inc to Atmos's proxy group, which was subsequently added to Atmos's proxy group in Rebuttal testimony.

¹³⁸ Attorney General Brief at 25.

¹³⁹ Attorney General at 22, footnote 97.

¹⁴⁰ Attorney General Brief at 27.

¹⁴¹ Attorney General Brief at 27–33.

¹⁴² Attorney General Brief at 33–34.

In its response brief, Atmos again reiterated its position that the Attorney General's DCF analysis contained faults including outdated data, incorporation of DPS growth rates, and duplication of S&P Capital IQ growth rates.¹⁴³ Atmos argued that in correcting these issues, the Attorney General's DCF analysis results would indicate ROEs of 9.80 percent to 10.01 percent.¹⁴⁴ Atmos also maintained its position that its RPM results are reasonable as compared to historically observed returns and risk premiums.¹⁴⁵ Additionally, Atmos argued that since both parties agree that the CAPM has its limitations in practice, using the ECAPM may provide a more accurate measure of the ROE than the traditional CAPM.¹⁴⁶ Finally, Atmos noted its disagreement with the Attorney General's assertions regarding non-utility proxy groups, size premiums, and flotation cost adjustments.¹⁴⁷

As discussed in recent cases, such as Case No. 2024-00092¹⁴⁸, 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, considerable variation exists in both data and application within each modeling approach, which can lead to very different results. The Commission's role is to

¹⁴³ Atmos's Post-Hearing Reply Brief (Atmos Response Brief) at 17.

¹⁴⁴ Atmos Response Brief at 17.

¹⁴⁵ Atmos Response Brief at 18.

¹⁴⁶ Atmos Response Brief at 19.

¹⁴⁷ Atmos Response Brief at 19-20.

¹⁴⁸ Case No. 2024-00092, *Electronic Application of Columbia Gas of Kentucky, Inc. For An Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; and Other Relief* (Ky. PSC Dec. 30, 2024) Order at 42.

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 multiple actions that can be and were taken into 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.

Although 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 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.¹⁴⁹ According to Attorney General witness Baudino, Atmos witness D’Ascendis developed the PRPM method, which Mr. Baudino states:

[I]s based on historical risk premium relationships that may or may not hold for the future. We do not really know if investors expect the variance of historical risk premiums to continue or if they even use this information to assist them in determining their required ROE. We also do not know if investors would model the PRPM using Mr. D’Ascendis’ assumptions.¹⁵⁰

¹⁴⁹ See Case No. 2021-00214, (Ky. PSC May 19, 2022), Order at 47–48; See also Case No. 2022-00372, *Electronic Application of Duke Energy Kentucky, Inc. for (1) An Adjustment of Electric Rates; (2) Approval of New Tariffs; (3) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; and (4) All Other Required Approvals and Relief* (Ky. PSC Oct. 12, 2023), Order at 41; Case No. 2024-00092, *Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; and Other Relief* (Ky. PSC Dec. 30, 2024), Order at 43.

¹⁵⁰ Baudino Direct Testimony at 46–47.

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 evaluate risk and returns both implicitly and explicitly.

The Commission reiterates that it also continues to reject the use of flotation cost adjustments, financial risk adjustments, and size adjustments in the ROE analyses.¹⁵¹ Atmos included a 0.06 percent increase in ROE for flotation costs, which are costs associated with the sale of new issuances of common stock, such as market pressure, underwriting fees, and out-of-pocket costs for printing, legal, and registration.¹⁵² Attorney General witness Baudino asserted that a DCF model using current stock prices should already account for investor expectations regarding the collection of flotation costs, and recovering flotation costs “essentially assumes that the current stock price is wrong and that it must be adjusted downward to increase the dividend yield and the resulting cost of equity.”¹⁵³ The Commission finds that Atmos has not established that flotation costs should be recovered through rates.

Regarding financial risk adjustment, Atmos adjusted its requested ROE 0.04 percent lower to account for decreased investor risk for Atmos for its better long-term issuer ratings compared to the Utility Proxy Group.¹⁵⁴ The Attorney General’s witness

¹⁵¹ See Case No. 2024-00092, Dec. 30, 2024 Order at 43.

¹⁵² D’Ascendis Direct Testimony at 4, 56.

¹⁵³ Baudino Direct Testimony at 60.

¹⁵⁴ D’Ascendis Direct Testimony at 54.

Baudino stated that this assertion of lower credit risk was inconsistent with Atmos's claim that it was a greater investor risk due to its size,¹⁵⁵ discussed below.

Regarding size adjustment, Atmos argued in favor of a 0.05 percent ROE increase to account for Atmos's smaller size compared to the Utility Proxy Group companies.¹⁵⁶ Atmos asserted that investors generally demand greater returns from smaller companies to offset increased risk that a smaller company will be unable to handle significant events that affect sales, revenues and earnings.¹⁵⁷ Attorney General witness Baudino countered that Atmos should not be treated as a small company because Atmos's size (not just its Kentucky operations) is comparable to the Utility Proxy Group companies—the Kentucky division does not issue its own debt or equity and therefore does not face risks independent of Atmos's overall financial stability.¹⁵⁸ The Commission finds that Atmos's ROE should not include a size adjustment.

After consideration of the evidence on record, the Commission finds that an ROE of 9.75 percent for Atmos's base rates and an ROE of 9.65 percent for its natural gas capital riders is fair, just and reasonable. Furthermore, ROE for capital riders is adjusted downwards because "[w]ith a rider, since a return is guaranteed and the time line of recovery is known and ordinarily not meaningfully delayed, the required return is less than

¹⁵⁵ Baudino Direct Testimony at 59.

¹⁵⁶ D'Ascendis Direct Testimony at 4, 46,

¹⁵⁷ D'Ascendis Direct Testimony at 46–47.

¹⁵⁸ Baudino Direct Testimony at 58.

the ROE associated with a rate case as the risk involved is decreased and most lag associated with recovery is eliminated.”¹⁵⁹

Capital Structure/Cost of Debt:

The Kentucky/Mid-States Division of Atmos Energy Corporation is not a separate legal entity and, therefore, all debt or equity funding of the operations it performs must be issued by Atmos Energy Corporation (Atmos Energy) as a whole, on a consolidated basis.¹⁶⁰ Atmos argued that, for this reason, it is appropriate to use Atmos Energy’s consolidated capital structure in setting rates for Atmos’s Kentucky customers.¹⁶¹ Therefore, Atmos proposed a capital structure comprised of 38.93 percent long-term debt, 0.19 percent short-term debt, and 60.88 percent common equity.¹⁶² This proposed capital structure is consistent with the 13-month actual capital structure for the period ending June 30, 2024.¹⁶³ Additionally, Atmos proposed a 4.11 percent weighted average cost of long-term debt, which excludes securitized debt issued in connection with Winter Storm Uri.¹⁶⁴ A summary of Atmos Energy’s modified cost of capital for Atmos follows:

¹⁵⁹ Case No. 2020-00060, *Electronic Application of Kentucky Utilities Company for Approval of Its 2020 Compliance Plan for Recovery by Environmental Surcharge* (Ky. PSC Sept. 29, 2020), Order at 20.

¹⁶⁰ Direct Testimony of Joe Christian (Christian Direct Testimony) at 7.

¹⁶¹ Christian Direct Testimony at 7–8.

¹⁶² Christian Direct Testimony at 8.

¹⁶³ Christian Direct Testimony at 8.

¹⁶⁴ Christian Direct Testimony at 8–9.

	Capital Ratio	Component Costs	Weighted Avg Cost
Short-Term Debt	0.19%	17.14%	0.03%
Long-Term Debt	38.93%	4.11%	1.60%
Common Equity	60.88%	10.95%	6.67%
Total Capital	<u>100.00%</u>		<u>8.30%</u>

In addition to reducing the ROE to 9.4 percent, the Attorney General recommended reducing Atmos's equity ratio from its proposed 60.88 percent to 52.5 percent.¹⁶⁵ The Attorney General explained that this recommendation is consistent with past Commission Orders, as well as recent requests from gas distribution companies.¹⁶⁶ Regarding Atmos's proposed equity ratio, the Attorney General argued that an equity ratio of 60.88 percent is unreasonable, excessive, and directly conflicts with the Commission's Order in the past rate case that Atmos's common equity ratio be reduced in subsequent a case toward the common equity ratio of a proxy group of companies.¹⁶⁷ The Attorney General's proposed capital structure results in a WACC of 8.30 percent and is as follows:¹⁶⁸

¹⁶⁵ Baudino Direct Testimony at 36.

¹⁶⁶ Baudino Direct Testimony at 36.

¹⁶⁷ Baudino Direct Testimony at 3.

¹⁶⁸ Direct Testimony of Randy Futral (Futral Direct Testimony), Table 4 at 24.

	Capital Ratio	Component Costs	Weighted Avg Cost
Short-Term Debt	0.19%	17.14%	0.03%
Long-Term Debt	47.31%	4.11%	1.94%
Common Equity	52.50%	9.40%	4.94%
Total Capital	<u>100.00%</u>		<u>6.91%</u>

In rebuttal, Atmos reiterated that it does not have a holding company and, therefore, its proposed capital structure represents an actual cost, rather than a hypothetical or subsidiary cost that is part of a larger holding company.¹⁶⁹ Atmos argued that its proposed capital structure is reflective of what is necessary for it to maintain its current credit metrics, which enable it to access long-term debt at more favorable terms.¹⁷⁰ Additionally, Atmos provided multiple analyses showing the effects of the Attorney General's recommended capital structure if it were applied to Atmos Energy as a whole.¹⁷¹ As a result of this analysis, Atmos concluded that the Attorney General's proposed capital structure would lead to a credit worthiness downgrade if Atmos's Kentucky operations represented the entirety of Atmos Energy.¹⁷² Atmos argued that it would be inappropriate to use Atmos Kentucky's approximate five percent representation of Atmos Energy as an excuse to not allow it to contribute ratably to Atmos Energy's overall financial performance.¹⁷³ Atmos also argued that the use of a hypothetical capital

¹⁶⁹ Christian Rebuttal at 3.

¹⁷⁰ Christian Rebuttal at 4.

¹⁷¹ Christian Rebuttal at 4.

¹⁷² Christian Rebuttal at 4 and Exhibit JTC-R-1.

¹⁷³ Christian Rebuttal at 4–5.

structure for ratemaking purposes with increased long-term debt would negatively affect its financial integrity, putting it at risk of a credit rating downgrade and increases to its cost of debt financing.¹⁷⁴ Atmos also provided an analysis which compared the savings that have been achieved since 2014 as a result of being ‘A’ rated by debt rating agencies, and the effect on these savings if it had been a ‘B’ rated company.¹⁷⁵ Atmos recomputed the imbedded long-term cost of debt which resulted in an overall cost of debt of 4.56 percent, and concluded that its cost of debt of 4.11 percent supported in this case resulted in savings of approximately \$1.14 million.¹⁷⁶ Atmos asserted that, if the Commission were to accept the Attorney General’s recommended capital structure, it would be appropriate to also utilize the higher cost of long-term debt rate of 4.56 percent.¹⁷⁷

Atmos argued further that its proposed common equity ratio of 60.88 percent falls within the range of the common equity ratios maintained by the Utility Proxy Group of 40.23 percent to 62.38 percent, for the fiscal year 2023. Atmos provided an additional comparison which examined the past eight quarters of average capital structures for the Utility Proxy Group, including and excluding short-term debt which range from 31.92 percent to 59.06 percent and 35.43 percent to 59.24 percent, respectively.¹⁷⁸ Additionally, Atmos considered Value Line’s projected capital structures for the proxy group which ranged from 42.50 percent to 61.00 percent for 2024-2029.¹⁷⁹ Finally, Atmos

¹⁷⁴ Christian Rebuttal Testimony at 4 and Exhibit JTC-R-1.

¹⁷⁵ Christian Rebuttal Testimony at 6 and Exhibit JTC-R-2.

¹⁷⁶ Christian Rebuttal Testimony at 6–7 and Exhibit JTC-R-2.

¹⁷⁷ Christian Rebuttal Testimony at 7.

¹⁷⁸ D’Ascendis Rebuttal Testimony at 6 and Exhibit DWD-2R at 1.

¹⁷⁹ D’Ascendis Rebuttal Testimony at 6 and Exhibit DWD-2R at 3.

surveyed the authorized equity ratios of natural gas utility companies from 2020 through the present, which ranged from 32.27 percent to 62.38 percent.¹⁸⁰ In consideration of these analyses, Atmos argued that the requested capital structure is consistent with the range of capital structures maintained by the Utility Proxy Group, and is appropriate to be used.¹⁸¹

In his brief, the Attorney General reiterated that Atmos's proposed common equity ratio is unreasonable, excessive, and recommended the Commission reject it.¹⁸² The Attorney General argued further that Atmos's requested common equity ratio is 20.5 percent higher than the proxy group average, and stands in sharp contrast to the Commission's final Order in Atmos's last rate case, in which the Commission ordered Atmos to reduce its equity ratio and placed Atmos on notice that in a subsequent rate case, the Commission might further reduce its common equity ratio to more closely approximate that of its peers.¹⁸³ The Attorney General argued that transferring more of Atmos's financing costs into long-term debt would reduce costs to Atmos and its ratepayers, and that Atmos did not provide evidence to support its concern of a ratings downgrade should it not receive its proposed capital structure and that this concern is mere speculation.¹⁸⁴ The Attorney General maintained that Atmos's proposed common

¹⁸⁰ D'Ascendis Rebuttal Testimony at 6 and Exhibit DWD-2R at 4.

¹⁸¹ D'Ascendis Rebuttal Testimony at 7.

¹⁸² Attorney General Brief at 20.

¹⁸³ Attorney General Brief at 20.

¹⁸⁴ Attorney General Brief at 21.

equity ratio is far beyond traditional norms, and exceeds its needs for its Kentucky operations.¹⁸⁵

In its brief, Atmos reiterated that its proposed common equity ratio reflects its actual capital structure, rather than a hypothetical common equity ratio as proposed by the Attorney General.¹⁸⁶ Atmos argued that the Commission's Order in its prior rate case is a clear outlier from decades of Commission precedent, as the Order approved a hypothetical capital structure for Atmos Energy, rather than an actual capital structure.¹⁸⁷ Atmos stated that, with an imposed hypothetical capital structure, Atmos Energy's Kentucky customers would not be contributing back ratably to the funds from operations at the same level as customers in Atmos Energy's other jurisdictions.¹⁸⁸ Atmos argued that Atmos Energy's current capitalization allows it to respond to emergencies in ways other utilities cannot, and that its strong balance sheet allows it to access the debt market at more favorable rates.¹⁸⁹ Atmos argued further that Atmos Energy's actual capital structure and strong balance sheet benefit Atmos Energy's Kentucky customers.¹⁹⁰

In its final brief, Atmos argued that the Attorney General's argument supporting its proposed capital structure relies solely on its proxy group comparison, and goes against Commission precedent of utilizing actual capital structures.¹⁹¹ Atmos again reiterated its

¹⁸⁵ Attorney General Brief at 22.

¹⁸⁶ Atmos Brief at 27-28.

¹⁸⁷ Atmos Brief at 28.

¹⁸⁸ Atmos Brief at 30.

¹⁸⁹ Atmos Brief at 30–31.

¹⁹⁰ Atmos Brief at 30.

¹⁹¹ Atmos Response Brief at 11.

argument that the Attorney General's proposed capital structure is purely hypothetical, and Atmos's proposed capital structure is its actual 13-month period end capital structure.¹⁹² Atmos also argued that the Attorney General's proposed capital structure would result in Atmos Energy's customers in other jurisdictions subsidizing Kentucky customers.¹⁹³

In the final Order of Case No. 2021-00214, the Commission voiced its concerns regarding the size of Atmos's common equity ratio.¹⁹⁴ In that case, the Commission found that Atmos's common equity ratio should be reduced to 54.50 percent, and noted that, in subsequent rate case filings, the Commission would review the proxy group common equity ratios and further transition down to the average common equity ratio of 50.0 percent or a median or average, whichever the facts merited.¹⁹⁵ Despite the Commission's findings in Case No. 2021-00214, Atmos proposed an even larger common equity ratio than the 57.05 percent it proposed in the prior case and, more importantly, failed to establish the reasonableness of that capital structure.

As an initial matter, the Attorney General's witness, Baudino, presented evidence that the average common equity ratio for the proxy group was 49.36 percent in 2023 and 49.79 percent in 2024 and is expected to be 48.71 percent for the 2027-2029 period.¹⁹⁶ Witness Baudino further noted that Columbia Gas of Kentucky requested a common equity ratio of 52.64 percent in its most recent rate case and that Delta Gas Company

¹⁹² Atmos Response Brief at 12.

¹⁹³ Atmos Response Brief at 15.

¹⁹⁴ Case No. 2021-00214, (Ky. PSC May 19, 2022), Order at 37.

¹⁹⁵ Case No. 2021-00214, Order at 38.

¹⁹⁶ Baudino Direct Testimony, Table 2 at 35.

requested a common equity ratio of 52.76 percent in its most recent rate case.¹⁹⁷ Atmos's witness responded to that evidence, in part, by asserting that Atmos's requested common equity ratio of 60.88 percent "falls within the common equity ratios maintained by the Utility Proxy Group."¹⁹⁸ However, a closer examination of the common equity ratios for the "Utility Proxy Group" in the table provided by Atmos's own witness indicated a range of common equity ratios from 37.55 percent to 47.17 percent in the third quarter of 2024, if Atmos is excluded from the group.¹⁹⁹ Moreover, Atmos's own witness indicated that those same companies, again excluding Atmos, had a range of common equity ratios from 37.55 percent to 55.08 percent in the third quarter of 2024 at the operating company level.²⁰⁰ Atmos's witness also indicated that the equity ratios of natural gas utility companies from 2020 through the present ranged from 32.27 percent to 62.38 percent,²⁰¹ but those companies are not as representative as the gas distribution companies included in his Utility Proxy Group. Further, even among those companies, equity ratios above 55 percent were unusual.²⁰² Thus, the evidence supports the Attorney General's position that Atmos's equity ratio is substantially higher than comparable utilities.

While Atmos asserts that its high equity ratio provides benefits, Atmos failed to present evidence indicating that those benefits justify the cost to customers of an unusually high equity ratio. Specifically, the Attorney General's witness indicated that

¹⁹⁷ Baudino Direct Testimony, at 36.

¹⁹⁸ D'Ascendis Rebuttal Testimony at 6.

¹⁹⁹ D'Ascendis Rebuttal Testimony, Exhibit DWD-2R at 1.

²⁰⁰ D'Ascendis Rebuttal Testimony, Exhibit DWD-2R at 2.

²⁰¹ D'Ascendis Rebuttal Testimony, at 6.

²⁰² See D'Ascendis Rebuttal Testimony, Exhibit DWD-2R at 4–6.

adjusting Atmos's capital structure to reflect a 52.5 percent equity ratio, all else being equal, would reduce the revenue requirement by about \$5.375 million.²⁰³ Conversely, in an attempt to reflect the benefits of Atmos's higher equity ratio, Atmos presented evidence that adjusting Atmos's capital structure to reflect a 52.5 percent equity ratio in the capital structure would increase borrowing costs on long term debt from 4.11 percent to about 4.56 percent and would therefore increase costs by about \$1.14 million annually,²⁰⁴ which was substantially lower than the savings reflected by the Attorney General. Thus, assuming the accuracy of Atmos's estimated cost, the benefits to customers of reducing the equity share of the capital structure to 52.5 percent, which were generally accurately reflected in the testimony presented by the Attorney General,²⁰⁵ would far exceed the cost in the form of an increased debt rate such that it would be unreasonable to choose that increased equity cost to achieve the claimed debt savings.²⁰⁶

While a change in the equity share of the capital structure could increase debt rates, Atmos's evidence did not establish that would occur in this case. Specifically, Atmos's analysis of the increased debt cost was premised on its position that its rating would fall from an A+, A, or A- to a BBB+, BBB, or BBB-, and it would suffer increased borrowing costs for debt it incurred from October 15, 2014, forward if it had an equity ratio

²⁰³ Futral Revised Testimony at 5.

²⁰⁴ Christian Rebuttal Testimony at 6–7.

²⁰⁵ The savings would be slightly reduced by the change in the return on equity approved herein, because the Attorney General calculated the savings before adjusting the return on equity. However, even with the lower return on equity approved in this case, the savings from reducing the equity ratio would be significantly higher than the costs alleged by Atmos.

²⁰⁶ Hearing Testimony of Richard A. Baudino (Baudino Hearing Testimony), May 7, 2025 HVT at 11:10:32.

of 52.5 percent.²⁰⁷ Atmos did not provide sufficient evidence to support that its rating would fall. In contrast, Atmos's actual common equity ratios in a 2013 rate case and a 2017 rate case were 49.16 percent and 52.57 percent.²⁰⁸ All things being equal, the common equity from those two prior cases would suggest that an equity ratio in the 50 percent range would not negatively affect Atmos's borrowing costs. That inference is further supported by common equity ratios of the utilities in the proxy group which have apparently generally found that a lower equity ratio is sufficient to support borrowing. Thus, the Commission finds that Atmos failed to establish that its proposed equity ratio of 60.88 percent is reasonable or provide sufficient benefit to ratepayers, or that reducing the equity ratio as proposed by the Attorney General would materially affect borrowing costs.

Further, there is nothing improper about the Commission adjusting a utility's capital structure for ratemaking purposes where the Commission finds that the utility's actual capital structure is unreasonable. Atmos, in making decisions regarding whether to raise capital through debt or equity issuances, or by retaining capital, controls its capital structure. If Atmos makes decisions with respect to its capital structure that unreasonably increase costs to customers, the Commission has the authority to make an adjustment to prevent unreasonable costs from being passed on to customers, and depending on the

²⁰⁷ See Christian Rebuttal Testimony, Exhibit JTC-R-2 Interest Savings; see also Baudino Hearing Testimony, May 7, 2025 HVT at 11:06:30-11:10:32 (discussing Mr. Christian's analysis).

²⁰⁸ See Case No. 2018-00281 (Ky. PSC May 7, 2019), Order at 33-34 (indicating the common equity ratios at the time of the 2013 and 2017 cases, when discussing how Atmos's actual common equity ratio has increased over the years); Baudino Hearing Testimony, May 7, 2025 HVT at 11:06:30-11:10:32 (explaining that Atmos's actual common equity ratios at the time of the 2013 and 2017 cases rebut Mr. Christian's claims that a reduction in the equity ratio would have actually changed the debt cost).

circumstances, may be required to do so.²⁰⁹ Further, the Commission has given Atmos significant notice that it was concerned with the reasonableness of Atmos's rising equity ratio.²¹⁰ However, Atmos failed to establish that its equity ratio in this case is reasonable for the reasons discussed above and in the evidence presented by the Attorney General. Thus, the Commission finds that Atmos's proposed capital structure, as filed, is not reasonable and does not result in fair, just, and reasonable rates for Atmos's consumers in Kentucky, and therefore, the Commission finds that an adjustment is necessary.

The Attorney General proposed to adjust the capital structure to reflect an equity ratio of 52.5 percent consistent with the capital structure of Columbia Kentucky and Delta. However, while there is some merit to the Attorney General's argument, the Commission finds that it would be more reasonable to reduce Atmos's common equity ratio to 53.50 percent, which is roughly between the equity ratios of those Kentucky LDCs and the highest recent common equity ratios at the operating level for companies, other than Atmos, in the Utility Proxy Group.²¹¹ The Commission notes that a 53.5 percent equity ratio, which is still on the higher end of the Utility Proxy Group, is an incremental step from the adjustment made in Atmos's last rate case. In subsequent rate filings, the

²⁰⁹ See KRS 278.030(1), indicating that a utility demand, collect and receive fair, just and reasonable rates for the services rendered or to be rendered by it to any person; KRS 278.040(1) indicating that the Commission shall enforce the provisions of KRS Chapter 278; see also KRS 278.270 stating "Whenever the commission, upon its own motion or upon complaint as provided in KRS 278.260, and after a hearing had upon reasonable notice, finds that any rate is unjust, unreasonable, insufficient, unjustly discriminatory or otherwise in violation of any of the provisions of this chapter, the commission shall by order prescribe a just and reasonable rate to be followed in the future."

²¹⁰ See Case No. 2018-00281 (Ky. PSC May 7, 2019), Order at 32-35, discussing Atmos's rising equity ratio, which had increase from 49.16 percent to 52.57 percent from 2013 to 2017, and then increased to 58.06 percent in 2018, before indicating that the Commission may make adjustments in future cases if Atmos did not bring the equity ratio down; see also Case No. 2021-00214, (Ky. PSC May 19, 2022), Order at 37-38.

²¹¹ See D'Ascendis Rebuttal Testimony, Exhibit DWD-2R at 2.

Commission will continue to review the proxy group common equity ratios and, if supported, will further transition down to an equity ratio based on the median or average ratio, as the facts merit.

Having reviewed the record and being otherwise sufficiently advised, the Commission finds, in this case, that Atmos's common equity ratio should be adjusted to 53.50 percent and that the equity balance adjusted out of the capital structure should be placed in long-term debt at Atmos's current average long-term debt rate of 4.11 percent.

Rate of Return Summary

Applying the cost rates of 17.14 percent for short-term debt, 4.11 percent for long-term debt, and 9.75 percent for common equity, the Commission revised capital structure percentages consisting of 0.19 percent, 46.31 percent, and 53.50 percent, respectively, produce an overall weighted cost of capital of 7.15 percent.

	Percent of Total	Cost Rate	13-month Avg. Cost
Short-Term Debt	0.19%	17.41%	0.03%
Long-Term Debt	46.31%	4.11%	1.90%
Common Equity	53.50%	9.75%	5.22%
Total Capital	100.00%		7.15%

RATE DESIGN

Cost of Service Study

Atmos filed three cost of service studies (COSSs), which are identified as the Customer/Demand study, the Demand-Only study, and the Energy/Demand Study.²¹²

²¹² Application, Direct Testimony of Paul H. Raab (Raab Direct Testimony) at 13.

The Customer/Demand study classifies investments in distribution mains as both customer- and demand-related, which reflects that the Company's level of investment in distribution mains is driven by the maximum demand that customers place on the system, but that there is also a minimum level of investments in distribution mains that would be necessary regardless of the level of such demand.²¹³ The Demand-Only study classifies investments in distribution mains as only demand-related.²¹⁴ The Energy/Demand Study classifies distribution main investment costs as both demand-related and commodity-related, based on the average and excess demand approach.²¹⁵

In the Customer/Demand study, Atmos utilized the minimum system approach. 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.²¹⁶ Although this concern has been expressed in electric rate cases, it was also expressed for natural gas²¹⁷ 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. Atmos stated that it did not perform a COSS utilizing the zero-intercept method in preparation of its rate case filing because the results of such a study have not been

²¹³ Raab Direct Testimony at 3.

²¹⁴ Raab Direct Testimony at 4.

²¹⁵ Raab Direct Testimony at 9.

²¹⁶ 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.

²¹⁷ 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).

reliable in the past and Atmos could not defend them.²¹⁸ The Attorney General's testimony did not address Atmos's COSSs and did not propose an alternate COSS.

Having reviewed Atmos's multiple COSSs, the Commission finds the evaluation of the results of the Customer/Demand study to not be reasonable. The Commission finds the Demand-Only study to be reasonable to use as a guide for revenue allocation and rate design. The Commission finds that Atmos should continue to file multiple COSSs in future base rate filings, including a COSS based upon the zero-intercept method for the allocation of distribution mains. If such study does not produce reasonable results, a COSS should be filed where distribution mains are allocated as 100 percent demand.

Revenue Allocation and Rate Design

For the revenue allocation, Atmos examined the minimum, maximum, and average revenue increases required by class to produce an equalized rate of return from the three studies.²¹⁹ Below illustrates the relative rate of return (ROR) at current rates and at Atmos's proposed rates.²²⁰

²¹⁸ Atmos's Response to Commission Staff's Fourth Request for Information (Staff's Fourth Request), Item 4(c).

²¹⁹ Raab Direct Testimony at 19.

²²⁰ Raab Direct Testimony, Exhibit PHR-2, page 1 of 75; Exhibit PHR-3, page 1 of 75; Exhibit PHR-4, page 1 of 75.

Rate of Return	Res	Non-Res Firm	Non-Res Interruptible	Transport Firm	Transport Interruptible	Total Company
Customer/Demand						
Current	0.23	2.00	22.29	4.35	26.57	1.00
Proposed	0.50	1.56	15.75	3.53	17.91	1.00
Demand Only						
Current	0.65	0.88	23.95	1.23	27.04	1.00
Proposed	0.78	0.85	16.90	1.29	18.22	1.00
Energy/Demand						
Current	0.91	1.20	1.92	0.55	1.77	1.00
Proposed	0.96	1.05	1.70	0.81	1.48	1.00

Atmos proposed no change in rate design, maintaining a monthly base customer charge and declining block volumetric rates for all rate schedules. Based on the results of the Demand-Only COSS, the Commission finds that the revenue allocation for the rate classes will be applied to the volumetric rates, where applicable, while the customer charges are within the range of reasonableness and will remain unchanged from the proposal. Based on the remaining revenue allocation, the Commission finds the volumetric charges for the G-1 Firm Sales Service to be reasonable as follows: \$1.6261 per Mcf for 0-300 Mcf, \$1.1390 per Mcf for 301-15,000 Mcf, and \$0.9817 per Mcf for over 15,000 Mcf.

In Case No. 2021-00214, the Commission denied Atmos's proposed increase to its monthly residential customer charge from \$19.30 to \$24.00 citing that the proposed increase would result in Atmos collecting one of the most expensive customer charges in the Commonwealth.²²¹ Additionally, the proposed increase would have occurred at a time when customers in Atmos's Kentucky service territory were recovering from a natural disaster.²²² Atmos's monthly residential customer charge was last adjusted to \$19.30 in

²²¹ Case No. 2021-00214, (Ky. PSC May 19, 2022), Order at 52-53.

²²² Case No. 2021-00214, (Ky. PSC May 19, 2022), Order at 53.

Case No. 2018-00281.²²³ Here, the Commission finds that the residential customer charge should increase to \$25.00 per billing period, which is an increase of \$5.70 from the current residential customer charge of \$19.30 per billing cycle. The Commission recognizes that Atmos will have a higher-than-average residential customer charge compared to other LDCs in Kentucky. However, the Commission also recognizes that Atmos's fixed costs have increased and that fixed costs can be higher for a utility that primarily serves rural customers, such as Atmos, due to serving low density areas where the number of meters per mile would be lower than those in higher density areas. A residential customer with an average monthly usage of 5.2 Mcf will experience an average monthly bill of \$33.73, which is an increase of \$6.38 or 23.34 percent from an average monthly bill of \$27.35 based on current rates.²²⁴

The Commission finds that the interruptible sales and interruptible transportation declining block volumetric rates should be revised as follows: \$0.9755 per Mcf for 0-15,000 Mcf, and \$0.8002 per Mcf for over 15,000 Mcf. The Commission finds the revisions to rates, which are outlined in Appendix B to this Order, are reasonable and should be approved.

Effective Date and Refund

On May 8, 2025, Atmos made a filing in which it provided the Commission notice pursuant to KRS 278.190(2) of its intent to place its proposed rates into effect, subject to refund, for service rendered on or after May 12, 2025, and in which it indicated that it

²²³ Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 7, 2019), at 51.

²²⁴ For the purpose of this Order, the average monthly bill at the current and proposed rate is calculated based on the customer charge and the per Mcf base rate. Additional line items, such as the Gas Cost Recovery rate and the PRP, are excluded from this average monthly bill calculation.

would maintain records for such refunds. The rates determined to be reasonable and approved herein are different from and lower than those proposed by Atmos, which were placed into effect for service rendered on or after May 12, 2025. Thus, the Commission finds that Atmos should refund to its customers all amounts collected in excess of the rates approved herein for service rendered on or after May 12, 2025, through the date of entry of this Order, and that the rates approved herein should be effective for service rendered on or after the date of entry of this Order.

RIDERS

Pipeline Replacement Program (PRP)

The Commission first approved Atmos's PRP rider in Case No. 2009-00354,²²⁵ allowing Atmos to receive accelerated recovery of costs associated with the replacement of bare steel pipeline, which presented a safety risk, over a period of 15 years at an estimated cost of \$124 million. However, due to greater than anticipated costs for the replacement of bare steel pipelines initially approved to be included in the PRP,²²⁶ the Commission determined in Case No. 2017-00349 that greater scrutiny of the PRP was necessary, and therefore, among other things, placed a \$28 million per year cap on capital spending for projects that could be included in the PRP,²²⁷ with the intent of shielding ratepayers from potentially unreasonable PRP costs.

²²⁵ Case No. 2009-00354, *Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 28, 2010), Order at 8.

²²⁶ Atmos discovered an additional 100 miles of bare steel pipeline to be replaced and underestimated replacement costs per mile by over 100 percent. Thus, by 2017, the estimated cost of the PRP had ballooned to \$438 million. See 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 37.

²²⁷ Case No. 2017-00349, (Ky. PSC May 3, 2018), Order at 40-42, stating "[t]he eligible bare steel pipeline replacements for which Atmos's PRP is approved, however, cannot reasonably be made and funded by ratepayers at the levels estimated by Atmos for the PRP program years of 2019 through 2022."

In response to the \$28 million cap on PRP spending, among other things, Atmos filed a forecasted rate case in Case No. 2018-00281 in which the Commission found that Atmos had simply shifted the capital it expected to spend on bare steel replacements in the PRP to other capital projects in base rates, which the Commission referred to as non-PRP projects.²²⁸ The Commission at that time was concerned with the pace of Atmos's capital spending and the need for the non-PRP projects, which Atmos asserted were necessary to address safety concerns, given that Atmos shifted capital expenditures to the non-PRP projects and effectively doubled spending on those projects largely because of the limit imposed on the PRP spending.²²⁹ The Commission found that Atmos failed to justify the need for some of those projects, and limited non-PRP capital spending used to determine rate base in that rate case to \$29.26 million, based on a 5-year historical average. Further, while the Commission stated that it was "not imposing a specific limit on Atmos's non-PRP capital spending in years after the forecasted test period [in that case]," the Commission indicated that in future cases "Atmos should scrutinize the justification for its projects closely and be prepared to provide supporting documentation showing how each project is consistent with its DIMP or TIMP [Transmission Integrity Management Program] . . . if its total non-PRP capital spending exceeds the 5-year rolling average."²³⁰

²²⁸ Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 7, 2019), Order at 18-19. The Commission noted that Atmos's non-PRP spending went from \$33.9 million in 2018 to \$58.7 million in 2019 and \$68.7 million in 2020, which the Commission noted was in addition to an increase from \$18.6 million in 2015 to \$34.2 million in 2016. Case No. 2018-00281, (Ky. PSC May 7, 2019), Order at 19.

²²⁹ Case No. 2018-00281 May 7, 2019 Order at 21–23

²³⁰ Case No. 2018-00281, May 7, 2019, Order at 24–25.

In Case No. 2021-00214, Atmos was permitted to include Alydl-A projects in the PRP on a case-by-case basis. In Case No. 2023-00231, the Commission increased the \$28 million cap on PRP projects to \$30 million but excluded specific Alydl-A projects that Atmos sought to include in that case.²³¹ In denying the inclusion of the Alydl-A projects at issue in that case, the Commission explained that:

Atmos did not indicate that the projects proposed herein ranked the highest on its DIMP or explain why they should be prioritized over specific projects that rank higher, including why the projects should be prioritized over higher ranking bare steel projects in this and subsequent years.²³²

While the Commission indicated that deviations from the DIMP were permitted based on specific facts, the Commission indicated that reference to Atmos's DIMP, which is prepared pursuant to a federal requirement that distribution system operators rank the risks to their distribution system,²³³ is important, because it offered a quick guide to ensure that Atmos was prioritizing projects that posed the greatest safety risk.²³⁴

In the present case, Atmos requests that: (1) All Aldyl-A pipe replacement be included for recovery under the PRP,²³⁵ (2) The PRP spending cap be removed or increased,²³⁶ and (3) The non-PRP spending cap, which Atmos contends was imposed by Case No. 2018-00281, be removed or increased.²³⁷

²³¹ Case No. 2023-00231, *Electronic Application of Atmos Energy Corporation for PRP Rider Rates Beginning October 1, 2023* (Ky. PSC Sept. 29, 2023), Order at 18.

²³² Case No. 2023-00231 (Ky. PSC Sept. 29, 2023), Order at 17.

²³³ See 49 C.F.R. § 192.1007.

²³⁴ Case No. 2023-00231 (Ky. PSC Sept. 29, 2023), Order at 16–18.

²³⁵ Application at 8.

²³⁶ Application at 6–7.

²³⁷ Application at 6–7.

Atmos argued that Aldyl-A should be included in the PRP, because Aldyl-A has been identified by both PHMSA and the Commission as posing a significant safety risk. Atmos noted that other Kentucky utilities have been authorized to address Aldyl-A replacement through similar capital recovery mechanisms and states that it seeks comparable treatment.²³⁸ Atmos also asserted that the ad-hoc, case-by-case analysis of whether Aldyl-A may be included in the PRP lacks clarity.

The Attorney General argued Atmos performed poorly in implementing its bare steel replacement through the PRP, which resulted in significant cost overruns and caused the Commission to impose limits on Atmos's PRP. The Attorney General asserts Atmos is still unable to give a clear timeline and costs estimates for its remaining bare steel replacement.²³⁹ The Attorney General argued that Atmos's implementation of its bare steel replacement through the PRP is evidence of how the Aldyl-A replacement will go, and stated that "[g]iven the cost uncertainties that exist in the pending bare steel program, the addition of a new replacement program on top of the existing one poses enormous rate risk for Atmos ratepayers."²⁴⁰ The Attorney General argued that the Commission should maintain its current approach, which allows Atmos to replace any project-specific section of Aldyl-A pipe if it is prioritized based on the DIMP.²⁴¹

Atmos argued that the PRP cap will not allow Atmos to replace bare steel pipeline within the original 15-year timeline.²⁴² Atmos estimated the remaining cost to replace

²³⁸ Atmos Post-Hearing Brief at 3.

²³⁹ Attorney General Post-Hearing Brief at 35–38.

²⁴⁰ Attorney General Post-Hearing Brief at 38.

²⁴¹ Attorney General Post-Hearing Brief at 38–39.

²⁴² Austin Direct Testimony at 42.

bare steel in the sum of \$144 million.²⁴³ Atmos estimated that the cost of replacing all Aldyl-A pipe would be \$243,697,545.²⁴⁴ Atmos argued that the non-PRP cap limits should be raised or removed to allow Atmos's budget to include all projects necessary to maximize safety, reliability, and economic growth.²⁴⁵ The Attorney General's witness Kollen countered that the caps are necessary to protect ratepayers from continuing cost overruns.²⁴⁶ He also asserted that the caps are not hard caps because Atmos is permitted to engage in additional spending if it justifies such spending.²⁴⁷

As the Commission has previously recognized, there are significant risks posed by Aldyl-A pipelines, particularly pre-1973 Aldyl-A pipelines, which according to evidence presented by Atmos make up a significant portion of the Aldyl-A pipe on its system. The Commission does share some of Attorney General's concerns with respect to expanding the scope of the PRP. However, case-by-case review of each project in the time anticipated by the PRP rider is difficult and may result in needed projects being excluded or not requested. Further, as discussed in more detail below, the Commission is maintaining an overall limit on annual PRP capital spending to protect ratepayers. The Commission also still expects Atmos to prioritize replacement of the existing pipe through the PRP based on potential safety risks and to follow its TIMP and DIMP when deciding replacement priority, unless specific circumstances justify deviating from the DIMP and TIMP (e.g. there is pipeline that is more risky but that risk is not reflected in the DIMP, or

²⁴³ Atmos's Response to Attorney General's First Request, Item 48(b).

²⁴⁴ Atmos's Response to Staff's Post-Hearing Data Request, Item 3, Exhibit Staff_PH_1-03_Att1.

²⁴⁵ Austin Direct Testimony at 27–28.

²⁴⁶ Kollen Revised Direct Testimony at 34.

²⁴⁷ Kollen Revised Direct Testimony at 35.

economic savings justify replacing lower risk pipe as part of another nearby project). If the Commission finds in later cases, particularly in later rate cases, that Atmos failed to prioritize replacement of the existing pipe through the PRP based on potential risk without justification, the Commission may eliminate or reduce the scope of Atmos's PRP, because the intent of the PRP is to prioritize projects based on safety by allowing for accelerated cost recovery outside of a rate case. The Commission believes that those limits and the risk to Atmos that the PRP may be eliminated are sufficient to address the very valid concerns raised by the Attorney General, though the Commission expects to review how Atmos's PRP is working, including how Atmos is prioritizing projects, in Atmos's next rate case. Thus, subject to the limits discussed herein, the Commission finds that Atmos should be permitted to include all Aldyl-A pipe replacement in the PRP.

With respect to Atmos's request to increase the annual PRP caps, the Commission finds that PRP spending caps remain necessary as a tool to prevent ratepayers from being subject to unlimited spending or from spending decisions that are not made on a deliberate, prioritized basis for reducing potentially dangerous pipe. However, the Commission recognizes that additional capital spending will be necessary on an annual basis to complete the replacement within a reasonable timeframe, especially since all Aldyl-A is now authorized to be included in the PRP. The Commission therefore finds that the PRP cap should be increased to \$40 million annually to keep up with cost increases and expedite safety measures.

In approving the increase in the PRP cap, the Commission notes that Atmos has repeatedly framed the PRP cap as an obstacle to meeting safety guidelines. However, nothing herein should be construed as preventing Atmos from completing projects to

replace bare steel or Aldyl-A beyond the annual PRP cap as necessary to provide safe, adequate, and reliable service. Such capital expenditures to replace bare steel or Aldyl-A beyond the annual cap may be recovered in future general rate cases. The PRP was developed as an incentive to encourage replacement of potentially hazardous pipeline—limiting accelerated recovery does not prevent Atmos from replacing all its bare steel and Aldyl-A pipe immediately. The limitations only prevent accelerated recovery of costs through the PRP to provide a check against cost overruns. In that regard, Atmos should also be prepared to demonstrate in future filings everything that it has done to determine accurate cost estimates and reduce the per unit actual costs for pipeline replacement. Atmos ratepayers cannot be expected to bear the entire burden of consequences for incorrect estimates and delays to the extent Atmos has the ability to plan and control those costs.

With respect to Atmos's request to increase the non-PRP spending, the Commission does not believe that the statements in Case No. 2018-00281 to which Atmos referred were intended to impose a specific cap on non-PRP spending in future periods. However, to the extent that was the intent of the language, the Commission is not maintaining an ongoing cap on non-PRP spending going forward. Atmos, like other utilities, may construct needed plant additions and replacements so long as they do not result in wasteful duplication,²⁴⁸ and Atmos otherwise complies with the provisions of KRS Chapter 278 and 807 KAR Chapter 5 such as requesting a CPCN where

²⁴⁸ KRS 278.020(1), in relevant part, prohibits a utility from constructing any plant, equipment, property, or facility without the Commission's approval, except for "ordinary extensions of existing systems in the usual course of business. The Commission will not grant a CPCN unless the utility establishes that the facility the utility intends to construct will not result in "wasteful duplication." *Kentucky Utilities Co. v Pub. Serv. Comm'n*, 252 S.W.2d 885 (Ky. 1952). Further, pursuant to 807 KAR 5:001, Section 15(3), a facility is not considered to be in the ordinary course of business if it results in wasteful duplication.

appropriate. Further, Atmos is entitled, pursuant to KRS 278.180 and 897 KAR 5:001, Section 16, among other statutes and regulations, to request a rate increase in its discretion to recover the reasonable costs of providing service. Thus, nothing herein should be construed as preventing Atmos from completing projects necessary for Atmos to furnish adequate, efficient and reasonable service or as preventing Atmos from requesting recovery of costs in future general rate cases.

In addition to the issues addressed above, the Commission makes the following findings regarding annual PRP filings to facilitate a prompt review of Atmos's annual PRP filings. Atmos should not propose changes to the methodology for calculating or applying the PRP mechanism in the annual PRP filings, because proposing such changes complicate and delay the review of the PRP filings. Changes to the methodology for calculating or applying PRP mechanism should only be proposed in rate cases or in separate applications. The Commission also finds that Atmos shall use the PRP ROE approved in this case in future PRP filings until its next rate case order. As a result, Atmos shall not be required to file ROE testimony as part of a PRP filing.²⁴⁹

Pipeline Modernization

Atmos also sought accelerated recovery of costs related to new federal Pipeline and Hazardous Materials Safety Administration (PHMSA) regulations, referred to as the Mega Rule, via a Pipeline Modernization (PM) Rider.²⁵⁰ Atmos proposed a mechanism

²⁴⁹ See Case No. 2022-00222, *Electronic Application of Atmos Energy Corporation to Establish PRP Rider Rates for the Twelve Month Period Beginning October 1, 2022* (Ky. PSC Mar. 25, 2023), Order at 24-25 (explaining how opening up the ROE in each annual PRP filing slowed down the processing of Atmos's PRP filings).

²⁵⁰ Application, Direct Testimony of T. Ryan Austin (Austin Direct Testimony) at 24.

similar to the PRP process, which would involve over \$48 million in spending over the next ten years.²⁵¹

The Attorney General recommended denying addition of the PM Rider and was concerned that it would be used broadly to circumvent non-PRP caps to replace Aldyl-A pipe or other present or future projects.²⁵² However, Atmos witness Ryan Austin testified that the intent of the PM Rider is only to cover pipeline testing and replacement of pipeline that cannot be tested in compliance with PHMSA in a cost-effective manner without replacing pipeline.²⁵³ Atmos provided a list of the projects it identified intending to recover for under the PM Rider, with projected project dates.²⁵⁴

The purposes of allowing accelerated recovery of an expense or capital expenditure are twofold: (1) to incentivize spending on a certain type of project, and (2) to simplify the process of approving spending on that type of project.²⁵⁵ The PRP incentivizes spending on projects intended to increase pipeline safety but not expressly required law. Atmos is required by PHMSA to perform testing, so the Commission need not provide Atmos any incentive to perform its federal statutory duties.

In addition, contrary to Atmos's PRP cases where the review process is simplified because Atmos has already established a uniform method for pipeline replacement, the

²⁵¹ Atmos's Response to Staff's Post-Hearing Request, Item 2, Attachment 1.

²⁵² Kollen Revised Direct Testimony at 44.

²⁵³ Hearing Testimony of T. Ryan Austin (Austin Hearing Testimony), HVT at 10:03:39.

²⁵⁴ Austin Direct Testimony, Exhibit TRA-5.

²⁵⁵ See Case No. 2009-00354, *Application of Atmos Energy Corporation for an Adjustment of Rates*, Application (filed Oct. 29, 2009), Direct Testimony of Gary L. Smith at 16, stating "the PRP mechanism will provide benefits to the customer by avoiding the costly and resource-intensive process necessary to review adjustments through the traditional rate case process replacing it instead with a simple, straightforward and financially transparent process." See also Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 7, 2019), Order at 14.

same uniform application does not apply to PHMSA compliance. In PRP cases, Atmos uniformly replaces bare steel with current industry standard pipeline material of the same size.²⁵⁶ The PRP process advances administrative efficiency because for each bare steel pipeline to be replaced, Atmos is not required to file an application for a CPCN, establish the need to replace bare steel, or establish that the replacement pipeline is the least-cost reasonable alternative to meet that need.

Improvements for PHMSA compliance require a more varied assessment of reasonable options that are necessary to comply with PHMSA and do not result in wasteful duplication.²⁵⁷ At hearing, Mr. Austin acknowledged four different options for complying with the PHMSA Mega Rule:²⁵⁸ (1) replacing pipeline that is incompatible with the inline inspection (ILI) tool; (2) retrofitting existing pipeline for ILI tool usage; (3) conducting pressure testing on existing pipeline and transporting in liquid natural gas to prevent outage while the pipeline is bypassed; and (4) reducing pressure to a level that would not trigger application of PHMSA Mega Rule requirements. Three of these four options are listed as proposed options for the proposed projects listed by Atmos.²⁵⁹ PHMSA-related replacement or testing involves too many variables for a one-size-fits-all process that is appropriate for PRP projects. The Commission must assess whether PHMSA requires action be taken, whether each option resolves that requirement, and the

²⁵⁶ Case No. 2018-00281, (Ky. PSC May 7, 2019), Order at 14; Application, Direct Testimony of Gregory W. Smith at 3.

²⁵⁷ See Case No. 2022-00084, *Electronic Application of Duke Energy Kentucky, Inc. for a Certificate of Public Convenience and Necessity Authorizing the Phase One Replacement of the AM07 Pipeline* (Ky. PSC Feb. 24, 2023), Order at 2.

²⁵⁸ Austin Hearing Testimony, HVT at 10:09:30.

²⁵⁹ Austin Direct Testimony, Exhibit TRA-5.

costs and benefits associated with each option. The Commission sees no advantage in treating projects that would normally require a CPCN as part of a streamlined process. The Commission notes that it previously permitted a similar rider as part of a settlement between Duke Kentucky and the Attorney General; however, Duke Kentucky was still required to file a CPCN for pipeline replacement projects outside the ordinary course of business.²⁶⁰

The Commission finds that in order to maintain consistency, Atmos's request to implement a PM Rider should be granted. However, as in the Duke Kentucky case, and in light of Atmos's previous failure to file CPCN applications when appropriate,²⁶¹ the Commission finds that any projects for which Atmos seeks to obtain accelerated recovery under the PM Rider must be approved via CPCN application. Furthermore, the PM rider shall be limited in scope to the projects listed in Exhibit TRA-5 to Mr. Austin's Direct Testimony.

Taxes

Atmos proposed a Tax Rider designed to capture the effects of federal income tax changes implemented by the Inflation Reduction Act of 2022 (IRA)²⁶² and other tax related costs that would change from the amounts included in the base revenue requirement, including the return on the Corporate Alternative Minimum Tax (CAMT) deferred tax asset and credits included in rate base and in the base revenue requirement.²⁶³ Atmos noted

²⁶⁰ 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 Dec. 28, 2021), Order at 5–6.

²⁶¹ Case No. 2018-00281, (Ky. PSC May 7, 2019), Order at 24–25.

²⁶² Public Law 117-169, 136 STAT. 1818.

²⁶³ Multer Direct Testimony at 6.

that the Tax Rider is also intended to capture future changes to the federal or state income tax rate and other federal, state, or local tax law changes, including changes in property tax rates.²⁶⁴

The Attorney General's witness argued that the Tax Rider is not necessary to capture tax changes and notes that Atmos only seeks accelerated recovery of tax increases, while the Commission implemented investigations to reflect decreases in the federal income tax rate following the Tax Cuts and Jobs Act.²⁶⁵ The Attorney General's witness also noted that there have historically been differences of opinion as to the calculation of deferred tax assets and deferred tax liabilities and that the Tax Rider would have the Commission preemptively delegate the authority for making such calculations to Atmos.²⁶⁶ He also argued that the property tax rate, which would be trued-up through the mechanism, is ill-defined and that a true-up mechanism is not necessary to reflect changes in that rate.²⁶⁷

Atmos's rebuttal testimony asserted that rejection of the rider would result in an unacceptable delay of application of tax changes, resulting in the filing of more frequent general rate cases.²⁶⁸

The Commission finds that implementation of a Tax Rider should be denied. Atmos has not met its burden of proof that the Tax Rider is necessary, and the Commission sees no justification for treating taxes differently than any other expense

²⁶⁴ Multer Direct Testimony at 6

²⁶⁵ Kollen Revised Direct Testimony at 36–37.

²⁶⁶ Kollen Revised Direct Testimony at 37.

²⁶⁷ Kollen Revised Direct Testimony at 38.

²⁶⁸ Multer Rebuttal Testimony at 20.

regarding the timing of recovery. Further, the mechanism as proposed is not well-defined and does not provide significant transparency over the true-up of tax changes.

Research & Development

The Attorney General supported eliminating an existing approximately \$300,000 per year recovered under the Research and Development (R&D) Rider, which provides a grant to the Research Technology Institute.²⁶⁹ The Attorney General witness asserted that ratepayers do not directly benefit from this and that these activities should be funded directly by the suppliers to the industry and manufacturers of industry and end-use customer equipment and appliances, both for competitive advantage and through their industry research organizations for safety and other reasons.²⁷⁰ Atmos countered that consistent with a NARUC resolution, the Commission previously chose to keep and increase the R&D rider despite Attorney General witness Kollen's recommendation against it.²⁷¹

The Commission finds that the R&D Rider should be retained. It may benefit safety and efficiency of gas infrastructure, and if removed, R&D costs may be passed through to ratepayers anyway via increased supplier costs.

IT IS THEREFORE ORDERED that:

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

²⁶⁹ Kollen Revised Direct Testimony at 48.

²⁷⁰ Kollen Revised Direct Testimony at 49.

²⁷¹ Rebuttal Testimony of Brannon C. Taylor (Taylor Rebuttal Testimony) at 27; 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 44.

2. The rates and charges as set forth in Appendix B to this Order are approved as fair, just and reasonable rates for Atmos, and these rates and charges are approved for service rendered on and after the date of entry of this Order.

3. Within 60 days of the date of service of this Order, Atmos shall refund to each customer all amounts collected from that customer in excess of the rates approved in this Order for service rendered on or after May 12, 2025, through the date of entry of this Order.

4. For PRP years beginning after the entry of this Order, Atmos's PRP rider shall be subject to a \$40 million annual recovery cap and shall allow the recovery of expenditures to replace bare steel and Aldyl-A pipeline. Atmos shall not propose changes to the PRP mechanism in its annual PRP filings. Atmos shall use the PRP ROE approved in this case in future PRP filings until the next rate case order.


5. Atmos's PM Rider is approved only for the projects listed in Exhibit TRA-5 to Mr. Austin's Direct Testimony. Projects to be initiated under this rider shall require a CPCN application to be approved prior to commencement of work. A CPCN shall not be required for any of these projects commenced prior to the issuance of this Order for which a CPCN would not otherwise be required.

6. Atmos's proposed tax rider is denied.

7. Within 20 days of the date of this Order, Atmos 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.

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

PUBLIC SERVICE COMMISSION


Chairman


Commissioner


Commissioner

ATTEST:

 
Executive Director



APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2024-00276 DATED AUG 11 2025

Atmos Energy Corporation - Kentucky Division Case No. 2024-00276 Test Year Ended March 31, 2026 \$ Millions	
	Rate Increase Amount
Atmos Requested Base Revenue Increase	\$ 33.001
Rate Base Adjustments	
Reduce Asset NOL ADIT to Reflect Updated Balances though FYE 2024	(0.085)
Reduce Asset NOL ADIT to Reflect Allocated Share of SSU Division Amount	(0.690)
Reduce Asset NOL ADIT to Reflect Taxable Income from Bridge Period	(0.062)
CWC - Adjustment 1 - Remove All Non-Cash Expenses	(1.045)
CWC - Adjustment 2 - Correct O&M, Non-Labor Expense Lag Days	(0.017)
Operating Income Adjustments	
Reduce Payroll Expense and Related Payroll Taxes Expense	(0.538)
Reduce Benefits Expense for Filing Error	(1.300)
Reduce Ad Valorem Expense	(3.030)
Remove American Gas Association and Kentucky Chamber of Commerce Dues	(0.078)
Rate of Return Adjustment	
Reflect Changes in Capital Structure (53.5% Equity and 46.5% Debt)	(4.729)
Reflect Return on Equity of 9.75%	(5.174)
Atmos-KY Composite Allocation Factor Update	
Reduction Due to FYE 2024 Composite Allocation Factor Update	(0.526)
Total Adjustments	<u><u>\$ (17.273)</u></u>
Base Rate Increase	<u><u>\$ 15.728</u></u>

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2024-00276 DATED AUG 11 2025

The following rates and charges are prescribed for the customers in the area 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

\$25.00	per meter per month for residential service
\$75.00	per meter per month for non-residential service

Distribution Charge

	\$ 1.6261 per Mcf
1-300 Mcf	\$ 1.1390 per Mcf
301-15000 Mcf	\$ 0.9817 per Mcf
Over 15000 Mcf	

RATE G-2 INTERRUPTIBLE SALES SERVICE

Base Charge

\$685.00	per delivery point per month
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Distribution Charge for Interruptible Service

1-15000 Mcf	\$ 0.9755 per Mcf
Over 15000 Mcf	\$ 0.8002 per Mcf

RATE T-3 INTERRUPTIBLE TRANSPORTATION SERVICE

Base Charge

\$685.00	per delivery point per month
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Distribution Charge for Interruptible Service

1-15000 Mcf	\$ 0.9755 per Mcf
Over 15000 Mcf	\$ 0.8002 per Mcf

RATE T-4
FIRM TRANSPORTATION SERVICE

Base Charge

\$685.00	per delivery point per month
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Distribution Charge for Firm Service

1-300 Mcf	\$ 1.6261 per Mcf
301-15000 Mcf	\$ 1.1390 per Mcf
Over 15000 Mcf	\$ 0.9817 per Mcf

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