

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

ILLINOIS COMMERCE COMMISSION	:	
On Its Own Motion,	:	
	:	
v.	:	06-0741
	:	
ATMOS ENERGY CORPORATION	:	
	:	
Reconciliation Of Revenues Collected	:	
Under Gas Adjusted Charges With Actual	:	
Costs Prudently Incurred	:	

COMPANY INITIAL BRIEF

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I. INTRODUCTION AND PROCEDURAL BACKGROUND

A. Introduction and Executive Summary

Atmos¹ prudently procured gas supply for the 2006 reconciliation period. Atmos procured gas supply contracts through a competitive bidding process that complies with the Act and all Commission rules. It analyzed the results of the bids it received through its RFP process, and it is undisputed that Atmos selected the lowest confirming bids available in each of its five operating zones. Atmos has demonstrated that its gas purchase costs were prudently incurred and therefore the Commission should order that they be recovered.

These procurements were done at a time when the market was in complete disarray as a result of two catastrophic hurricanes in the Gulf of Mexico. Atmos took this supply shock into account when evaluating the bids it received for the 2006 ACA period. The bids for gas supply in 2005 and 2006 were higher (relative to the requested index price) than they were in prior years. Given the market disruption, this change in available pricing was no surprise to the Company. However, Atmos also believed that the bids it selected for gas supply were reasonable and competitive given the Company's understanding of the marketplace. It was therefore also not surprising to the Company that the price it paid for baseload gas under the 2005 Contract was the lowest of the Comparable Utilities identified by Staff and under the 2006 Contract were the second lowest of the Comparable Utilities.

¹ The parties agreed upon standardized definitions for this proceeding. A copy of those definitions is attached as Addendum A. Unless otherwise specified, capitalized terms are defined as set forth in Addendum A.

Staff initially believed that the Company paid a higher price for baseload gas than any of the Comparable Utilities. When the Company showed that Staff's understanding of the pricing data was incorrect, the Company believed that Staff ought to have agreed with the Company that its gas procurements were prudent and that its costs should be recovered.

However, Staff has recommended two adjustments relating to the Company's supply contracts. The first would impose a price reduction for baseload gas purchased under the 2005 Contract and the 2006 Contract equal to the Adder—in effect requiring the Company to purchase gas at a price lower than any party was offering to sell to it and in fact at a price that was significantly lower than any of the Comparable Utilities paid for gas during this time period. The second adjustment would in effect require the Company to obtain a peaking service at no cost. Again, no vendor would offer to provide free peaking service to the Company.

Staff makes certain minor criticisms of the Company's RFP process, but does not identify any causal link between its criticisms and any real-world result—as shown above, Staff's position effectively would require the Company to obtain pricing that is simply not available in the real world. The prudence standard recognizes that reasonable minds can differ and the Company has presented a rational basis for each of its decisions. For example, the Company believed it could obtain a lower price by requesting bids for full system requirements due to economies of scale. While Staff would have taken a different approach, seeking separate bids from vendors for baseload delivery and peaking service does not render the Company's RFP process imprudent.

B. Procedural Background

On November 21, 2006, the Illinois Commerce Commission (“*Commission*”) entered an Order Commencing PGA Reconciliation Proceedings, in accordance with the requirements of Section 9-220² of the Public Utilities Act (the “*Act*”),³ which directed Atmos to present evidence at a public hearing to show the reconciliation of revenues under its Purchased Gas Adjustment (“*PGA*”) clause with the actual costs of such gas supplies prudently purchased for the 12 months ended December 31, 2006.⁴

The Company posted its notice of the filing of its direct testimony and exhibits in the Company’s business offices and was published in newspapers having general circulation in the Company’s gas service territory, in the manner prescribed by 83 Ill. Adm. Code 255, in compliance with the Commission’s November 21, 2006 order in this proceeding. No petitions to intervene were filed in this proceeding.

On May 1, 2012, an evidentiary hearing was held at the Commission’s offices at 527 E. Capitol, Springfield, Illinois. Appearances were entered by counsel on behalf of Atmos and Staff of the Commission⁵. The Company presented the testimony of Mark A. Martin, Vice President—Rates and Regulatory Affairs of the Company, Kentucky/Mid-States Division. Staff presented the testimony of Mary H. Everson an Accountant in the Accounting Department of the Financial Analysis Division of the Commission, Mark Maples, Senior Gas Engineer in the Engineering Department of the Energy Division of the Commission, and David Rearden, Senior Economist of the Energy Division of the

² 220 ILCS 5/9-220.

³ 220 ILCS 5/1-101 et seq.

⁴ Initiating Order.

⁵ Tr. (May 1, 2012) at 16:9-17:3.

Commission.⁶ At the conclusion of the hearing on May 1, 2012 the record was marked “Heard and Taken.”⁷

II. RESOLVED ISSUES

A. Lost Gas

Staff witness Everson proposed an adjustment for gas lost as a result of third party damage. Ms. Everson disagreed with the Company’s practice of recording reimbursements as miscellaneous revenue.⁸ Instead, Ms. Everson recommended that reimbursements in the amount of \$2,350 be recorded as an offset to recoverable gas cost in the PGA.⁹ Mr. Martin testified that the Company has agreed to the adjustment for lost gas proposed by Ms. Everson.¹⁰

B. NGPL Refunds

Staff witness Everson proposed an adjustment of \$375 for refunds received by the Company from Natural Gas Pipeline Company (“NGPL”) that were not reflected in the Company’s reconciliation.¹¹ Mr. Martin testified that the Company has agreed to the adjustment to include refunds from NGPL in its reconciliation.¹²

III. CONTESTED ISSUES

The disputed issues in the docket are centered on whether two gas supply contracts entered into by the Company for the Harrisburg operating zone were prudent.

⁶ See Company Ex. 2.0-2.5; Company Ex. 3.0; Company Ex. 4.0-4.6; Staff Ex. 1.0 - 4.0.

⁷ Tr. at 88:5-8.

⁸ Staff Ex. 1.0 at 3:37-43; Staff Ex. 1.0, Schedule 1.2.

⁹ *Id.*

¹⁰ Company Ex. 3.0 at 2:38-41.

¹¹ Staff Ex. 1.0 at 3:45-50; Staff Ex. 1.0, Schedule 1.3.

¹² Company Ex. 3.0 at 2:38-41.

Staff did not raise any issues with respect to gas procurement for the Company's four other operating zones of Virden, Vandalia, Metropolis, and Salem.¹³ For that reason, only the Company's Harrisburg operating zone is discussed in this brief unless otherwise noted. As described in more detail below, the price Atmos paid for gas under the 2005 Contract and the 2006 contract was fair, reasonable and competitive and among the lowest prices paid by the Comparable Utilities served by TETCO.¹⁴

A. Applicable Legal Standard

In accordance with Section 9-220¹⁵ of the Act, the Commission may authorize an increase or decrease in rates and charges based upon changes in the cost of purchased gas through the application of a purchased gas adjustment clause.¹⁶ Section 9-220(a) requires the Commission to initiate annual public hearings "to determine whether the clauses reflect actual costs of . . . gas . . . purchased to determine whether such purchases were prudent, and to reconcile any amounts collected with the actual cost of . . . gas . . . prudently purchased."¹⁷ In each such proceeding, the burden of proof is on the utility to establish the prudence of its applicable costs.¹⁸

Both the Commission and the Illinois Appellate Courts have defined prudence as the standard of care which a reasonable person would be expected to exercise under the same circumstances encountered by utility management at the time decisions had

¹³ Tr. (May 1, 2012) at 75:7-10.

¹⁴ Company Ex. 4.0 23:466-472.

¹⁵ 220 ILCS 5/9-220.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.*

to be made.¹⁹ In determining whether a decision was prudently made, only those facts available at the time judgment was exercised can be considered.²⁰ Hindsight review is impermissible in the context of a prudence determination.²¹

B. Gas Supply Contracts

The evidence in the record demonstrates that the Company prudently entered into the 2005 Contract and the 2006 Contract. The purchases under those contracts were used to provide service to customers and the Company has a right to be reimbursed for those purchases under the PGA clause. First, the Company had appropriate and reasonable gas supply procurement procedures in place in compliance with all applicable law.²² Second, the Company utilized these procedures and acted in accordance with the Act and Commission rules to select the lowest available bids.²³ The discussion to follow describes in greater detail the prudent steps the Company took to procure gas supply for Harrisburg.

1. Atmos Used Prudent Gas Supply Procedures

Atmos had prudent gas supply procurement procedures in place that it utilized to award the 2005 Contract and the 2006 Contract.²⁴ Mr. Martin testified that the Company issues RFPs, evaluates the bids it receives and selects the best bid in accordance with

¹⁹ *Illinois Commerce Comm'n v. Ill. Power Co.* 245 Ill. App. 3d 367 (Ill. App. 1993); *Illinois Commerce Comm'n v. Ill. Power Co.*, Docket No. 03-0699 at 3 (Order, Sept. 26, 2006)

²⁰ *Id.*

²¹ *Id.*

²² Company Ex. 2.1.

²³ Company Ex. 2.0 at 6:109-112.

²⁴ *Id.* at 3:56-5:95.

the Company's procedures for gas supply procurement.²⁵ Atmos filed excerpts of its RFP procedures as Exhibit 2.1.²⁶

Mr. Martin testified that Atmos maintains a list of qualified RFP recipients that meet certain minimum requirements.²⁷ Atmos reviews and updates this list annually.²⁸ The Company then sends a letter to qualified RFP participants setting forth the terms of the RFP, including the quantity of gas required, the serving pipeline, the length of the contract and information necessary for potential vendors to respond with qualifying bids.²⁹ Following the deadline for submission of bids, the Company analyzes each proposal received in comparison to any other proposals, taking into account the supplier/marketer's reputation, reliability of supply, and price.³⁰ Atmos also compares the differences between each proposal and some purchase standard, usually a supply plan, with careful attention being paid to different proposed pricing points, demand charges flexibility and cost.³¹

For the time period at issue (and in general), the Company selected the vendor that proposed the least expected cost.³² Mr. Martin testified the Company's procedures are designed to ensure the Company obtains competitive prices, terms and conditions

²⁵ *Id.*

²⁶ Company Ex. 2.1; Company Ex. 2.0 at 3:56-5:95.

²⁷ Company Ex. 2.0 at 4:67-73.

²⁸ *Id.* at 4:73-74.

²⁹ *Id.* at 4:77-80.

³⁰ *Id.* at 4:81-83.

³¹ *Id.* at 4:83-5:86.

³² *Id.* at 5:87-91.

for the purchase of gas.³³ The procedures comply with all applicable laws and regulations, including the Act and the Commission's rules.³⁴ No party has suggested otherwise. The Company followed prudent gas supply procurement procedures for all of its purchases affecting the 2006 reconciliation period.

2. Atmos Prudently Awarded Gas Supply Contracts

Atmos prudently awarded gas supply contracts by following its reasonable gas supply procurement procedures and selecting the lowest bids available.³⁵ With respect to the 2006 Contract, it is undisputed that the Company selected what it expected to be the lowest bid of the two bids it analyzed. Staff witness Rearden initially testified that he had difficulty determining if the Company's comparison of bids for the 2006 Contract was reasonable absent documentation of how the Company documented its price estimates.³⁶ During cross-examination, Staff witness Rearden agreed that this documentation has been provided.³⁷ The comparative analysis submitted by the Company confirms that the Company selected the bid it expected to be the lowest for the 2006 Contract.³⁸

The RFP for the 2006 Contract requested a bundled package of services to include up to 4,700 Dth per day MDQ firm city gate delivered natural gas supply during the term of the agreement and a 10-day firm city gate delivered peaking service up to

³³ *Id.* at 5:92-93.

³⁴ *Id.* at 5:93-95.

³⁵ Company Ex. 2.0 at 5:98-106; Company Ex. 4.0 at 16:323-338; Company Ex. 4.2; Company Ex. 4.3.

³⁶ Staff Ex. 3.0 at 10:201-203; Staff Ex. 4.0 at 3:48-52; Tr. at 77:4-78:5.

³⁷ Tr. at 78:6-79:16.

³⁸ See Company Ex. 4.2; Company Ex. 4.3.

2,900 Dth/day.³⁹ The RFP solicited bids for gas supply based on the ETX price index.⁴⁰ The 4,700 Dth/day could be made up of FOM daily quantities (to be nominated by the Company prior to the beginning of each month) and daily quantities (to be nominated by the Company on a day-ahead basis).⁴¹ The 10-day peaking supply was for the winter months December 2006 through February 2007 (to be nominated by the Company on a day-ahead basis).⁴²

For the 2006 Contract, the Company received three bids, one of which was rejected for nonconformance because it failed to provide anywhere near the quantity of gas stated in the RFP and required to meet the needs of the Harrisburg customers.⁴³ The only fully conforming bid was AEM's proposal.⁴⁴ A second proposal was non-conforming because it failed to quote the preferred price index specified in the RFP, IFGMR ETX.⁴⁵ Instead, the second bid proposed the alternate index point IFGMR Texas Eastern M3.⁴⁶ This bidder is referred to as the "M3 Supplier" to protect confidentiality. The M3 Supplier's proposal had two additional shortcomings that the M3 Supplier agreed to rectify by modifying its bid; however, the pricing remained at the

³⁹ Company Ex. 4.0 at 13:251-254.

⁴⁰ Company Ex. 2.0 at 7:135-139.

⁴¹ Company Ex. 4.0 at 13:254-257.

⁴² *Id.* at 13:257-259.

⁴³ Company Ex. 3.0 at 230-231; Company Ex. 4.0 at 13:260-266.

⁴⁴ Company Ex. 4.0 at 13:262-263.

⁴⁵ *Id.* at 14:266-14:268.

⁴⁶ *Id.* at 14:276-280.

alternate index point.⁴⁷ To facilitate analysis of the competitive bids, the M3 Supplier's proposal was considered for further evaluation along with the fully conforming bid.⁴⁸

The Company prepared an annualized cost comparison of the bid components including supplier demand charges and commodity pricing for the estimated normal annual purchase quantities.⁴⁹ This analysis was filed as Exhibit 4.2.⁵⁰ Because of the nonconforming bid, the M3 Supplier's proposal had to be evaluated using the historical pricing of the alternate index.⁵¹ Mr. Martin testified that the Company's comparative analysis reviewed historic IFGMR ETX and IFGMR Texas Eastern M3 index prices for the period January 2003 through September 2006.⁵² This review revealed that the ETX index price was lower than the M3 index price in every historic month of the period examined.⁵³ The Company's annualized cost comparison estimated that AEM's proposal would result in approximately \$450,000 less gas cost per year than the M3 Supplier's proposal.⁵⁴ Mr. Martin testified that a subsequent review of the annualized cost comparison revealed a calculation error.⁵⁵ However, the correction of this error would not have changed the result of the RFP because the corrected analysis estimates

⁴⁷ *Id.* at 14:269-275.

⁴⁸ *Id.* at 14:276-280.

⁴⁹ *Id.* at 14:281-285.

⁵⁰ Company Ex. 4.2.

⁵¹ *Id.* at 14:276-280.

⁵² Company Ex. 4.0 at 17:342-344.

⁵³ *Id.* at 17:344-347.

⁵⁴ *Id.*; Company Ex. 4.0 at 15:313-316.

⁵⁵ Company Ex. 4.0 at 16:323-335.

even greater savings under the 2006 Contract with AEM.⁵⁶ The corrected annualized cost comparison estimated that AEM's proposal would result in savings of more than \$500,000 in comparison to the M3 Suppliers proposal.⁵⁷ The Company filed the corrected annualized analysis as Exhibit 4.3.⁵⁸

Because the Company used prudent bid evaluation procedures, it comes as no surprise that the Company's estimated gas cost savings ended up being close to the actual cost savings realized.⁵⁹ Mr. Martin testified that review of actual commodity pricing indicated ratepayers saved approximately \$450,000 under AEM's proposal, which is right in line with the Company's analysis.⁶⁰ Of course, the prudence of the Company's actions are evaluated at the time they were made, but it may provide the Commission some comfort to know that the prudently-made evaluations were borne out by actual results.⁶¹

For the 2005 Contract, AEM was the sole bidder.⁶² However, as indicated in the record, all the protections of competitive bidding remained in place because AEM did not know it would be the only bidder.⁶³ This is borne out by the fact that the price for

⁵⁶ *Id.*

⁵⁷ *Id.*

⁵⁸ Company Ex. 4.3.

⁵⁹ See Company Ex. 4.2; Company Ex. 4.0 at 22:452-459.

⁶⁰ Company Ex. 4.0 at 22:452-459.

⁶¹ Of course, if there had been significant differences in market prices or volume purchased, actual results could have varied significantly from the projections, although this would not have affected the prudence of the procedures.

⁶² Company Ex. 2.0 at 5:100.

⁶³ *Id.* at 6:120-123.

baseload gas did not change in later RFPs and that the price the Company paid for baseload gas under the 2005 Contract was the lowest of the Comparable Utilities.

Atmos analyzed the 2005 Contract bid and determined that AEM's bid was competitive and reasonable.⁶⁴ This analysis took into consideration Atmos' knowledge of the market at the time the RFP was entered into.⁶⁵ Obviously, the Company was aware that the price of the bid was higher than in prior years. The Company understood that the market was in disarray as a result of two major hurricanes causing extensive damage in the Gulf of Mexico.⁶⁶ Additionally, Mr. Martin testified that the Company was familiar with the pricing generally available in the marketplace on TETCO as well as other pipes at the time the RFPs were made.⁶⁷ Based on all of the foregoing facts, the Company had substantial reasons to find it prudent to enter into the 2005 Contract. The Company believed that the price it was paying under the 2005 Contract, given its understanding of market conditions, was reasonable. This belief is borne out by the fact that the Company had the lowest cost of gas among Comparable Utilities for the 2005 Contract and the second lowest cost of gas for the 2006 Contract.⁶⁸

C. Specific Adjustments Proposed by Staff

Staff witness Rearden proposed two adjustments to the price the Company paid under the 2005 Contract and the 2006 Contract.⁶⁹ First, Staff witness Rearden alleges

⁶⁴ *Id.* at 5:100-102.

⁶⁵ *Id.* at 9:181-10:193.

⁶⁶ Tr. at 33:1-34:5.

⁶⁷ Tr. at 58:7-13.

⁶⁸ See Company Ex. 4.5; Company Ex. 4.6.

⁶⁹ Staff Ex. 3.0 at 11:224-12:231.

the price paid by Atmos for baseload gas was too high.⁷⁰ Second, Staff witness Rearden alleges that the price of the peaking service procured by the Company was too high.⁷¹

Neither of the two adjustments proposed by Staff witness Rearden are supported by the record and do not rebut or undermine the strong showing of prudence by the Company. Nor is there record support for the alternate pricing relied on by Staff to calculate their proposed adjustments. As previously discussed, the Company has established the prudence of its gas purchases, the use of prudent gas procurement procedures, and by selecting the lowest bids available to it under its competitive bidding process.⁷² Staff seeks to disallow costs from the utility whose prices were among the lowest of all Comparable Utilities for the period in question.⁷³ Neither of the two adjustments proposed by Staff witness Rearden should be adopted.

1. Baseload Price

Staff witness Rearden postulates that the price the Company paid for gas under the 2005 Contract and 2006 Contract represented an unreasonable price increase from the price the Company paid the prior year and therefore that an adjustment to the price paid in a contract entered into in 2004 should apply.⁷⁴ The evidence in the record does not support this adjustment. Staff witness Rearden admitted he reached his conclusion that the Company paid too high a cost for baseload gas without providing any evidence

⁷⁰ *Id.*

⁷¹ *Id.*

⁷² See *infra* at § III.B; *Id.* at 5:87-91; Company Ex. 4.2; Company Ex. 4.3.

⁷³ See Company Ex. 4.5; Company Ex 4.6.

⁷⁴ Staff Ex. 3.0 at 5:73-79; *id.* at 11:224-12:231.

of what a reasonable price increase would be.⁷⁵ There is no evidence to support a finding that the cost of gas should not have changed between 2004 and 2005—an unsupported conclusion particularly when one considers the substantial evidence pointing to significant changes in index differentials due to Hurricanes Katrina and Rita.⁷⁶

Under the 2005 Contract and the 2006 Contract, the Company paid a price for baseload gas of the FOM ETX plus the Adder pursuant to Section 3.2 of the 2005 Contract and the 2006 Contract (“Adder”).⁷⁷ Staff complains that the Adder is too high and proposed that a price of FOM ETX flat would have been reasonable.⁷⁸ This price was not available in the marketplace to the Company.⁷⁹ Nor was this price available to any other Comparable Utility.⁸⁰ The Company selected the lowest bids available to it under its competitive bidding process.⁸¹ If ETX Flat had been available, the Company would have selected it.⁸² Staff’s adjustment attempts to unreasonably impose a prudence baseline that was not available in the marketplace.

The availability of a price at one point in time does not mean that price will continue to be available in the future.⁸³ Even Staff witness Rearden has admitted that,

⁷⁵ Tr. at 81:16-19.

⁷⁶ Company Ex. 2.0 at 8:181-9:199; Tr. at 33:1-34:5.

⁷⁷ Company Ex. 2.4 at § 3.2; Company Ex. 2.5 at § 3.2.

⁷⁸ Staff Ex. 3.0 at 5:73-79.

⁷⁹ Company Ex. 3.0 at 13:257-263.

⁸⁰ Company Ex. 4.0 at 20:406-410.

⁸¹ See *infra* at § III.B; *Id.* at 5:87-91; Company Ex. 4.2; Company Ex. 4.3.

⁸² Company Ex. 3.0 at 13:257-258.

⁸³ Company Ex. 3.0 at 13:257-363.

in general, he believes gas prices change over time.⁸⁴ The gas marketplace was experiencing severe volatility during the period in question.⁸⁵ Mr. Martin testified that at the time the RFPs were issued, the marketplace was in disarray.⁸⁶ Specifically, Mr. Martin testified that a major hurricane in the Gulf of Mexico called Hurricane Katrina caused extensive damage to offshore gas platform.⁸⁷ Shortly thereafter, the Gulf of Mexico was again disrupted by Hurricane Rita.⁸⁸ Staff's assumption that FOM ETX flat was a reasonable price for the 2006 reconciliation period is unreasonable in light of the strong evidence presented by the Company that the marketplace was experiencing severe volatility.

Staff witness Rearden appears to suggest that utilities can obtain gas at flat index prices.⁸⁹ However, even Staff witness Rearden admits that utilities commonly enter into contracts with suppliers with adjustments (adders or discounts) to the index price.⁹⁰ Mr. Martin also testified that index adders are commonplace in the gas marketplace and further noted it is necessary to take into account the basis differential when determining whether a particular index pricing is reasonable.⁹¹ Because of the volatility in the market place due to Hurricane Katrina and Hurricane Rita, forward prices

⁸⁴ Tr. at 82:4-6.

⁸⁵ Company Ex. 2.0 at 9:181-187.

⁸⁶ *Id.*; Tr. at 33:7-17.

⁸⁷ Tr. at 33:7-22.

⁸⁸ *Id.*

⁸⁹ Staff Ex. 3.0 at 5:73-78; *Id.* at 11:218-221; Tr. at 83:22-84:5.

⁹⁰ Tr. at 84:6-15.

⁹¹ Tr. at 60:21-61:7.

for ETX were trading at a significant discount to Louisiana and NYMEX-based prices.⁹² Based on this marketplace knowledge, the Company determined that entering into a contract with a price of ETX plus the Adder was a prudent decision.⁹³

Staff's argument that the Adder was too high incorrectly focuses solely on the Adder without taking into consideration the index used and ignores the fact that index adders were changing during the period at issue due to changing differentials between indices.⁹⁴ Mr. Martin explained that often which index and adder is used is not truly important other than as a means to compare market pricing.⁹⁵ The Company used its knowledge of the marketplace to prudently determine that the 2005 Contract and the 2006 Contract offered reasonable pricing.⁹⁶

The prudence of this decision was borne out through examination of the pricing paid by Comparable Utilities. The FOM prices paid by the Comparable Utilities ranged from a NYMEX flat to NYMEX minus \$.21/Dth as well as a Gas Daily Texas Eastern M1 plus \$.10/Dth and an Inside FERC Henry Hub plus \$.16.⁹⁷ Despite the fact that the 2005 Contract and the 2006 Contract had a higher Adder than the Comparable Utilities, the Company actually paid the lowest price of gas under the 2005 Contract and the second lowest under the 2006 Contract.⁹⁸ This highlights the need to focus on the index in addition to the adder. Although there is no Commission requirement to obtain the lowest

⁹² Company Ex. 2.0 at 9:181-10:199.

⁹³ *Id.*

⁹⁴ See Company Ex. 4.0 at 4:77-82.

⁹⁵ Company Ex. 2.0 at 9:172-180.

⁹⁶ Company Ex. 2.0 at 9:181-10:193.

⁹⁷ Company Ex. 4.0 at 20:406-409.

⁹⁸ See Company Ex. 4.5; Company Ex. 4.6.

pricing of all other utilities, the fact that the Company did demonstrates the pricing was reasonable.⁹⁹

Having demonstrated that the record fully supports a finding that the Company prudently supplied Harrisburg with gas in 2006, the remainder of this Section addresses specific criticisms made by Staff witness Rearden and the disincentive for utilities to benefit ratepayers that would result if Staff's proposed adjustment were adopted.

a. Staff's Proposed Adjustment Creates a Disincentive to Obtain the Lowest Price

The emphasis Staff places on the Adder in determining the prudence of the 2005 Contract and the 2006 Contract creates a negative incentive for utilities to obtain the lowest pricing.¹⁰⁰ If the Commission were to adopt Staff's proposed adjustment, a utility might have an incentive to avoid contracts with adders that the utility reasonably believes to be the least expensive. If the utility faced a potential disallowance if it did not select the bid with the lowest adder, the utility might include a restriction in its future RFP terms that no bidder can specify an adder. This would be counterproductive because there is nothing wrong with an adder, and the Company has demonstrated that bids based on a historically lower index with an adder can result in lower overall gas supply costs to Illinois customers than bids based on an index with no adder. The Company advocates that its method of evaluating and comparing the entirety of the bid components and their impact on total gas cost is prudent and superior to Staff's tunnel-vision approach of simply looking at an adder. The Commission has previously tried to

⁹⁹ See Company Ex. 4.0 at 22:460-466.

¹⁰⁰ See Staff Ex. 3.0 at 5:73-79 (Staff views the adder in the 2005 Contract and 2006 Contract as unreasonable, but a contract without an adder reasonable).

avoid creating negative incentives for utilities to benefit ratepayers.¹⁰¹ In Docket No. 94-0040, the Commission sought to avoid creating a negative incentive for utilities to avoid system renewal by only disallowing the portion of cost in excess of the amount deemed prudent, rather than disallowing all costs.¹⁰² Likewise, in Docket No. 01-0701, the Commission explicitly noted that it did not want to discourage utilities from entering contracts spanning more than one reconciliation period if doing so produces a better result for ratepayers.¹⁰³ The Commission should continue its prior history of avoiding the creation of disincentives to benefit ratepayers and reject Staff's Adjustment.

b. Staff Incorrectly Claims There is No Alternate Pricing Comparison Available

Staff witness Rearden testified that "there is nothing else in the record to base an alternate price on."¹⁰⁴ Staff witness Rearden alleges this is true even if AEM's bid was the lowest in 2006 (which following cross-examination Staff appears to no longer dispute).¹⁰⁵ This is incorrect. As Mr. Martin testified, the Company can award a gas supply contract to AEM only if AEM submits the lowest bid.¹⁰⁶ The fair market price is

¹⁰¹ See *Ill. Commerce Comm'n v. Cent. Ill. Light Co.*, Docket No. 94-0040 (Order, Dec. 12, 1994) (seeking to avoid creating a disincentive to perform system renewal); *Ill. Commerce Comm'n v. Ill. Power Co.*, Docket No. 01-0701 at (Order, Feb. 19, 2004) (seeking to avoid creating an incentive to avoid more beneficial contracts).

¹⁰² See *Ill. Commerce Comm'n v. Cent. Ill. Light Co.*, Docket No. 94-0040 (Order, Dec. 12, 1994) ("refusing to place at least a portion of CILCO's investment into rate base would likely cause companies who discover dangerous situation to put off renewal even longer and to attempt to continue repairing the system even when that approach is, perhaps, not the most economical solution.").

¹⁰³ *Ill. Commerce Comm'n v. Ill. Power Co.*, Docket No. 01-0701 at (Order, Feb. 19, 2004) (noting that the Commission does not want to discourage utilities from entering into contract that overlap reconciliation periods if doing so produces better results to customers).

¹⁰⁴ Staff Ex. 4.0 at 10:212-214.

¹⁰⁵ Staff Ex. 4.0 at 10:210-217; Tr. at 77:21-79:16.

¹⁰⁶ Company Ex. 4.0 at 22:442-443.

established by the market composed of willing buyers and sellers.¹⁰⁷ For the 2006 reconciliation period, that fair market resulted from the RFP process undertaken by Atmos to determine the least cost bid for gas supply in its five operating zones.¹⁰⁸ AEM submitted the lowest bids for one of these operating zones, Harrisburg.¹⁰⁹ For the operating zones in which a non-affiliate submitted the lowest bid, Staff is willing to accept the fair market price as established by the market.¹¹⁰ However, in the Harrisburg operating zone in which AEM submitted the lowest bid, Staff claims it is unable to determine the real fair market price.¹¹¹

The Comparable Utility pricing data presents an additional basis for determining an alternate price. As previously discussed, Atmos paid the lowest price of gas under the 2005 Contract and the second lowest under the 2006 Contract.¹¹² Although Atmos is not required to obtain the lowest pricing of all other utilities, the fact that Atmos did is another basis for determining the pricing was reasonable.¹¹³ The evidence in the record demonstrates that not only was there an alternate price, but that the alternate price was significantly higher than the price paid by Atmos for gas as indicated by prices actually paid by other utilities and the rejected bid that was actually submitted in the RFP.

c. Atmos' RFP Procedures were Prudent

¹⁰⁷ Company Ex. 4.0 at 22:443-444.

¹⁰⁸ *Id.* at 22:444-446.

¹⁰⁹ *Id.* at 22:446-47.

¹¹⁰ *Id.* at 22:447-449.

¹¹¹ *Id.* at 22:449-451.

¹¹² See Company Ex. 4.5; Company Ex. 4.6.

¹¹³ See Company Ex. 4.0 at 22:460-466.

Staff witness Rearden complained that the Company imprudently eliminated potential bidders from its RFP list.¹¹⁴ This assertion is not supported by the record. Even Staff witness Rearden admits that it is unknowable whether more bids would have been received if the Company used an affirmative option instead of a negative option.¹¹⁵ As Mr. Martin discussed in his surrebuttal testimony, Staff witness Rearden appears to be operating under a mistaken assumption that Atmos removed entities from its RFP mailing list for not bidding in one year.¹¹⁶ This is not true.¹¹⁷ The Company only eliminated entities on the mailing list that had never bid and also failed to state their interest in ever doing so.¹¹⁸ Suppliers with even a marginal or potential interest would have confirmed to the Company their desire to remain on the list and receive further RFPs.¹¹⁹ Atmos' RFP process merely removed the entities that expressed no interest in bidding.¹²⁰ There is no evidence to suggest that using a negative option rather than an affirmative option (particularly where there were no automatic deletions of any bidder) would have had an effect on the number of bids received.¹²¹

Staff witness Rearden claims removing entities from the mailing list resulted in fewer bidders over time starting with 2003.¹²² The facts show that Staff witness

¹¹⁴ Staff Ex. 4.0 at 8:173-9:188.

¹¹⁵ *Id.* at 9:180-182.

¹¹⁶ Company Ex. 4.0 at 6:104-114.

¹¹⁷ *Id.*

¹¹⁸ *Id.*

¹¹⁹ *Id.*

¹²⁰ *Id.*

¹²¹ Company ex. 3.0 at 11:222-223.

¹²² Staff Ex. 4.0 at 8:166-167; Tr. at 80:3-80:20.

Rearden's assertion is incorrect. Mr. Martin testified that the Company received more bids in the 2006 RFP (three) than it did in the 2003 RFP (two) and the 2004 RFP (one).¹²³ Yet Staff considers the price obtained by the 2004 RFP to be prudent and alleges that the price obtained by the 2006 RFP is imprudent.¹²⁴

Staff witness Rearden additionally complained that Atmos should not have rejected the nonconforming bid.¹²⁵ Mr. Martin testified to several prudent reasons why the Company could not accept the nonconforming bid.¹²⁶ First, the Company was unable to allow one party to bid assuming unique supply parameters because it would be unfair to other bidders, undermine the integrity of the RFP process, and ultimately lead to higher prices for ratepayers.¹²⁷ Second, the nonconforming bid only represented a fraction of the baseload requirement in the RFP, and none of the peaking requirement.¹²⁸ The Company would have had to seek new bids with lower quantities, which would have likely resulted in higher prices or the potentially disastrous situation where the conforming suppliers declined to bid on the lower quantities.¹²⁹ Third, Mr. Martin testified the Company solicited RFPs for full system requirements because the Company believes this will yield better pricing through economies of scale than through piecemeal solicitation.¹³⁰ Fourth, Mr. Martin testified the Company believes bidders will

¹²³ Company Ex. 4.0 at 6:115-120; See Staff Ex. 3.0 at 7:137-8:140.

¹²⁴ Staff Ex. 3.0 at 5:73-79.

¹²⁵ *Id.* at 9:166-174.

¹²⁶ Company Ex. 4.0 at 19:387-20:409.

¹²⁷ *Id.* at 19:387-391.

¹²⁸ *Id.* at 19:392-399.

¹²⁹ *Id.*

¹³⁰ *Id.* at 19:400-409.

be less likely to bid or bid a higher price on RFPs with open-ended terms than with specific terms.¹³¹ Based on the factors considered by the Company, the evidence in the record demonstrates it was reasonable for the Company to reject the nonconforming bid.

d. Delivered Service

Staff witness Rearden asserted that the Company's use of delivered service instead of having transportation capacity was imprudent.¹³² Yet even Staff witness Rearden concedes that neither delivered service or transported service is always low cost.¹³³ In fact, the Company demonstrated that the decision to rely on delivered service actually saved the customers money over time.¹³⁴ The Company filed a comparison between the supplier demand charges from November 2003 through December 2006 to the demand charges the Company would have paid to hold the same necessary pipeline capacity on TETCO.¹³⁵ This analysis showed a savings in excess of one million dollars over this limited period of time.¹³⁶ Mr. Martin testified that he believed there would be similar savings both prior to and after that period.¹³⁷

Staff witness Rearden does not really dispute that the Company did in fact save money over time, although he does point out that it is difficult to ascertain the amounts

¹³¹ *Id.*

¹³² Staff Ex. 3.0 at 5:80-6:107.

¹³³ Staff Ex. 4.0 at 4:80-81.

¹³⁴ Company Ex. 4.0 at 10:184-200; Company Ex. 4.1.

¹³⁵ *Id.*

¹³⁶ *Id.*

¹³⁷ Company Ex. 4.0 at 10:197-200.

with a good degree of certainty.¹³⁸ Staff witness Rearden correctly points out that each approach has pros and cons that may outweigh cost savings.¹³⁹ However, the prudence standard recognizes that reasonable minds can disagree, and that more than one course of action given any particular set of facts may be prudent.¹⁴⁰ Since neither delivered service or transport capacity is clearly better, the Company's (or more particularly, its predecessor's) decision to rely on delivered service cannot be found imprudent, especially when the Company showed that there would be reason to believe that it would be less expensive than maintaining its own pipeline capacity.¹⁴¹

Staff witness Rearden further opined that an adjustment may be justified if costs during the 2006 reconciliation period increased even if the decision to release transportation capacity saved money over time.¹⁴² Notwithstanding Atmos' showing that it prudently incurred costs in 2006, the Commission has previously suggested that evidence of net savings over multiple years may not result in an adjustment in a year involving higher costs.¹⁴³ Staff's suggestion to consider the costs of one year without acknowledging any potential benefits is cherry-picking.¹⁴⁴ However, as Mr. Martin

¹³⁸ See Staff Ex. 4.0 at 6:109-7:138; Company Ex. 4.0 at 8:159-162.

¹³⁹ Company Ex. 4.0 at 8:162-9:167.

¹⁴⁰ *Ill. Commerce Comm'n v. Ill. Power Co.*, Docket No. 03-0699 at 3 (Order, Sept. 26, 2006) ("The prudence standard recognizes that reasonable persons can have honest differences of opinion without the one or the other necessarily being 'imprudent.'").

¹⁴¹ Company Ex. 4.0 at 8:162-9:167.

¹⁴² Staff Ex. 4.0 at 5:88-90.

¹⁴³ See *Ill. Commerce Comm'n v. Ill. Power Co.*, Docket No. 01-0701 at 7 (Order, Feb. 19, 2004) (noting that had the utility presented evidence of net savings, the result may have been different).

¹⁴⁴ Company Ex. 3.0 at 8:161-168.

testified, this assumes there is a cherry to pick.¹⁴⁵ As previously discussed, the Company's cost of gas was among the lowest of the Comparable utilities and Staff has no basis to allege the price of gas was too high.¹⁴⁶

e. TETCO Capacity Release

Staff witness Rearden alleges that the Company's predecessor was imprudent to release capacity on TETCO. More than fourteen years ago, before Atmos was operating in Illinois, its predecessor, United Cities, held four TETCO firm transportation and storage contracts.¹⁴⁷ At the time, Woodward Marketing, L.L.C. ("*Woodward*") was controlled by J.D Woodward, with a minority interest held by United Cities.¹⁴⁸ In 1996, United Cities made a decision to release its transportation capacity and instead take delivered service.¹⁴⁹ Starting in September 1996, two of the transportation contracts were terminated and Woodward did not obtain this released capacity.¹⁵⁰ Woodward did obtain the interstate pipeline capacity released by United Cities to TETCO under the other two contracts.¹⁵¹ Later, Atmos acquired United Cities.¹⁵² Eventually, Atmos indirectly acquired Woodward as a wholly owned subsidiary which became AEM.¹⁵³

¹⁴⁵ *Id.*

¹⁴⁶ See Company Ex. 4.5; 4.6.

¹⁴⁷ Company Ex. 4.0 at 11:215-217.

¹⁴⁸ Company Ex. 3.0 at 7:141-144.

¹⁴⁹ Company Ex. 4.0 at 11:220-221.

¹⁵⁰ *Id.* at 11: 217-218.

¹⁵¹ *Id.* at 11:218-222.

¹⁵² Company Ex. 3.0 at 7:139-146.

¹⁵³ *Id.*

Staff witness Rearden alleges that not holding transportation capacity resulted in Atmos' RFP process becoming monopolized by AEM.¹⁵⁴ The evidence demonstrates this assertion is incorrect. Mr. Martin testified that the Company issued fifteen RFPs for its five operating zones for the three calendar years between the years 2004-2008.¹⁵⁵ Mr. Martin testified that the number of times AEM submitted winning bids was comparable to the number of times non-affiliate bidders submitted winning bids.¹⁵⁶ In addition, the Company submitted evidence that Atmos has obtained gas supply from twelve different suppliers on TETCO between November 1997 through 2006.¹⁵⁷ These suppliers included TransCanada, PG&E, Engage, ProEnergy, SoNat Marketing, Woodward, Aquila Energy, Anadarko, OG&E, Energy USA, Duke Energy, and AEM .¹⁵⁸ The wide variety of different suppliers demonstrates that Atmos' RFP process has not been dominated by one entity.

More importantly, Staff witness Rearden has generally agreed that no evidence of a causal relationship between the previous decade's capacity release and a price change had been demonstrated.¹⁵⁹ In fact, the Commission has found the prices the Company has paid for gas to be reasonable in the decade leading up to the 2005 Contract.¹⁶⁰ Staff witness Rearden's speculation on this issue relies on an assumption

¹⁵⁴ Staff Ex. 3.0 at 8:155-160.

¹⁵⁵ Company Ex. 4.0 at 12:229-244.

¹⁵⁶ *Id.*

¹⁵⁷ Company Ex. 2.2.

¹⁵⁸ *Id.*

¹⁵⁹ Staff Ex. 4.0 at 8:162.

¹⁶⁰ Company Ex. 3.0 at 8:147-153.

that the Company received fewer bids over time.¹⁶¹ This reliance is improper for two reasons. First, the assumption is ungrounded because the number of bids actually increased during the 2006 RFP in comparison to prior years.¹⁶² Second, the bidding entities had no knowledge of the number of bids the Company was receiving.¹⁶³ Therefore, bidding entities could not bid a very high price as suggested by Staff witness Rearden because the bidding entity would risk losing the contract.¹⁶⁴ Further, what Staff considers to be a high price in this docket was actually the lowest price paid by any of the Comparable Utilities under the 2005 Contract and the second lowest under the 2006 Contract.¹⁶⁵

In any case, Staff's review of the capacity release in this proceeding is inappropriate in this docket. Without any evidence of a causal relationship between the capacity release and a price increase, Staff asks the Commission to review the prudence of a decision made fourteen years ago by a company that no longer exists through personnel that cannot be called to testify.¹⁶⁶ It is unclear how the Commission could conduct a fair review of that decision. In light of the lack of evidence of a causal relationship, and the strong record support that AEM did not monopolize the Harrisburg market, the Commission should decline to consider the 1996 capacity release in this docket.

¹⁶¹ See Staff Ex. 4.0 at 8:162-170.

¹⁶² Company Ex. 4.0 at 6:115-120.

¹⁶³ *Id.* at 9:172-175

¹⁶⁴ *Id.* at 9:175

¹⁶⁵ Company Ex. 4.5; Company Ex. 4.6.

¹⁶⁶ Company Ex. 3.0 at 9:169-174.

f. Comparable Utility Data is Relevant

a. Background

Atmos' use of pricing data for three Comparable Utilities in this docket is not irrelevant to this proceeding. In fact, it was Staff that first raised the issue of comparing the Company's costs to those of utilities deemed comparable by Staff. In Docket 05-0738, Staff testified in the Company's 2005 PGA proceeding that Atmos paid a high price for gas and alleged that Comparable Utilities paid a far lower price.¹⁶⁷ The Company believed that Staff's characterization was inconsistent with the Company's knowledge of the gas market. Accordingly, Atmos obtained the actual pricing data from Staff through a data request.¹⁶⁸ The Company's analysis of the data showed that Staff had misunderstood the data and in fact Atmos paid the lowest of the comparable utilities under the 2005 Contract and the second lowest under the 2006 Contract.¹⁶⁹

Staff's reliance on Comparable Utility data in the 2005 PGA docket suggests that Staff views this type of information as useful and relevant. During the evidentiary hearing, Mr. Lannon suggested that Staff viewed the Comparable Utilities information as a useful hindsight comparison because it is not a utility and therefore the prudence standard is not applicable to Staff.¹⁷⁰ Staff's claim that it is allowed to rely on hindsight

¹⁶⁷ Tr. at 46:13-22; See *Ill. Commerce Comm'n v. Atmos Energy Corp.*, Docket No. 05-0738, Exhibit 2.0 at 35:729-734.

¹⁶⁸ Tr. at 47:4-15.

¹⁶⁹ *Id.* at 46:18-22; Company Ex. 4.5-4.6.

¹⁷⁰ Tr. at 55:15-22.

review is incorrect. In fact, the prohibition on the use of hindsight review has primarily been invoked against Staff (and intervenors).¹⁷¹

All of this misunderstands the prohibition on hindsight review. The Company has shown through ample evidence that its decisions were prudent when made, and not subject to second guessing based on facts that later come into existence. No one is advocating a test whereby the ability to recover what it paid for gas would require that utility to prove that, for example, it paid a below-average price per dekatherm. That would be too stringent and unfair a test. However, it does not make sense for the Commission to deny recovery to a utility that would actually have passed that test.

a. Atmos had General Knowledge of the Pricing Available

In addition, the Comparable Utility data is not hindsight review because Atmos was familiar with the pricing generally available in the marketplace on TETCO as well as other pipelines at the time the RFPs were made.¹⁷² Mr. Martin testified that the Company determined it was a prudent decision to enter into the 2005 Contract and the 2006 Contract based on its knowledge of the market.¹⁷³ This means that even if the exact pricing data of the Comparable Utilities was not known at the time the RFP was made, the Company was generally aware of the pricing available at the time and based

¹⁷¹ See *Business and Professional People for the Public Interest v. Ill. Commerce Comm'n*, 146 Ill. 2d 175, 209 (1991) (discussing the rationale for the hindsight prohibition is to avoid placing an additional burden on the utility); *Ill. Commerce Comm'n v. Ill.*¹⁷¹ See *Ill. Commerce Comm'n v. Ill. Power Co.*, Docket No. 01-0701 at 23 (Order, Feb. 19, 2004) (rejecting use of hindsight review by Staff); *Illinois Commerce Comm'n v. Commonwealth Edison*, Docket No. 95-0119 (Order, Nov. 5, 1998)(finding that an intervenor relied on impermissible hindsight review); *But See Ill. Commerce Comm'n v. Cent. Ill. Light Co.*, Docket No. 99-0468 (Order, July 5, 2001) (rejecting use of hindsight by a utility).

¹⁷² Tr. at 58:7-13.

¹⁷³ Company Ex. 2.0 at 9:181-10:193.

its decision on this knowledge. The actual data learned later confirms the Company's view.

b. Non-prudence Uses

Staff takes an unnecessarily limited view by incorrectly assuming the Comparable Utility data does not have additional uses beyond determining prudence. For instance, Staff appears to believe utilities should be able to obtain gas at a flat index price.¹⁷⁴ However, the Company has presented evidence that the cost of gas may be lower under a gas supply contract that sets pricing based on an index and an adder.¹⁷⁵ Due to changing market conditions, no particular index is always better priced than another; therefore, it is necessary to consider basis differential between indices when comparing market pricing.¹⁷⁶ The Company considers understanding basis differentials to be a basic principle of the marketplace, and illustrated this principle through an example that in the context of banking that an interest rate of Prime minus 1% may not be favorable over an interest rate of Libor plus 2%.¹⁷⁷ The pricing data of the Comparable Utilities in this instance is another illustration of this principle – most of the Comparable Utilities had adjustments to their indices.

Additionally, the Commission could use the Comparable Utilities pricing data as a way to show that, regardless of the prudence of the Company's entering into the 2005 Contract and the 2006 Contract (which has been amply demonstrated), there was no harm to ratepayers that resulted from either contract. The Comparable Utility data is

¹⁷⁴ Staff Ex. 3.0 at 5:73-78; *Id.* at 11:218-221; Tr. at 83:22-84:5.

¹⁷⁵ Company Ex. 2.0 at 9:172-180.

¹⁷⁶ *Id.*

¹⁷⁷ *Id.*

particularly relevant in light of Staff's allegations that there is a lack of alternate pricing data to compare with the 2005 Contract and the 2006 Contract.¹⁷⁸ Staff has suggested using the price of FOM ETX from a prior year's contract as a baseline.¹⁷⁹ The fact that no Comparable Utility was able to obtain Staff's recommended baseline pricing is a relevant way to demonstrate that Staff's baseline was unavailable.¹⁸⁰

g. Summary

The record fully supports a finding that Atmos prudently procured its gas. The Company's has demonstrated that AEM was only selected as the winning bid after the Company correctly determined AEM was the lowest bidder. Moreover, the price Atmos paid for gas was reasonable, competitive and in line with the price paid by Comparable Utilities. The prudence standard acknowledges that reasonable minds can differ, and the Company has demonstrated a rational and prudent basis for each of the decisions and procedures Staff has disagreed with. Staff's adjustment unreasonably asks the Commission to require Atmos to obtain a price for gas that was not available in the marketplace and should not be adopted.

2. Peaking

A finding that Atmos prudently procured peaking service is fully supported by the record. As part of the Company's gas supply procurement process, the Company forecasted that it would need to provide 4700 Dth MDQ on any given day, and that it would need the option to take an additional 2900 Dth on ten days during the winter

¹⁷⁸ See Staff Ex. 4.0 at 10:206-217.

¹⁷⁹ *Id.*

¹⁸⁰ See Company Ex. 4.0 at 20:412-415.

period.¹⁸¹ The option to take the additional 2900 dekatherms on ten days during the winter period is referred to as peaking service and is a common way to address the fact that demand for natural gas depends on unpredictable weather.¹⁸²

AEM provided the peaking service under the 2005 Contract for the specified peaking period of November 2005 through March 2006.¹⁸³ AEM provided the peaking service under the 2006 Contract for the period December 2006 through February 2007.¹⁸⁴ Thus for the period at issue, the peaking service was available in January, February, March and December 2006. No party has disputed the need for the peaking service or that customers benefitted from the service. Instead, Staff witness Rearden complained that the Company paid too high a cost for its peaking service and proposed an adjustment that does not permit Atmos to recover any costs that it paid in ensuring availability through the purchase of peaking service.¹⁸⁵

Staff witness Rearden's proposed adjustment is not supported by the record or the law and should not be adopted by the Commission. As with the other provisions in the 2005 Contract and the 2006 Contract, the terms of the peaking service were obtained through the Company's competitive bidding process in accordance with the Act and the Commission's rules.¹⁸⁶ The Company analyzed the bids it received and

¹⁸¹ Company Ex. 2.0 at 14:293-306.

¹⁸² *Id.*

¹⁸³ *Id.* at 15:308-314.

¹⁸⁴ *Id.*

¹⁸⁵ Staff Ex. 3.0 at 14:272-291.

¹⁸⁶ Company Ex. 2.0 at 15:316-318.

selected the bid it believed to represent the lowest bid as a whole.¹⁸⁷ For the 2006 RFP, the other qualifying bidder priced its peaking service somewhat lower than AEM.¹⁸⁸ The Company took this into consideration when evaluating the bids, but the difference was not significant enough to make the overall contract more favorable to the Company.¹⁸⁹ As a whole, the AEM offer was better.¹⁹⁰ No party disputes this.

Staff witness Rearden suggests that the Company should not have bundled the peaking service with baseload and incremental purchases.¹⁹¹ However, the Commission recognizes that reasonable minds can differ, and the Company had a reasonable basis for believing bundling the system requirements would result in a lower overall price.¹⁹² As previously discussed, the Company believed RFPs for full system requirements could yield better pricing through economies of scale than through piecemeal solicitation.¹⁹³

The Company has demonstrated that its purchase of peaking service was reasonable and benefitted its customers. Staff witness Rearden's proposed disallowance is unreasonable. As much as the Company would like to pay lower prices

¹⁸⁷ *Id.* at 15:318-320.

¹⁸⁸ Company Ex. 3.0 at 14:290-295.

¹⁸⁹ *Id.*

¹⁹⁰ *Id.*

¹⁹¹ See Staff Ex. 3.0 at 14:272-277.

¹⁹² See *Ill. Commerce Comm'n v. Ill. Power Co.*, Docket No. 03-0699 at 3 (Order, Sept. 26, 2006) ("The prudence standard recognizes that reasonable persons can have honest differences of opinion without the one or the other necessarily being 'imprudent.'"); Company Ex. 4.0 at 19:387-20:409.

¹⁹³ Company Ex. 4.0. at 19:400-409.

for any service, it will never be able to obtain any service for free.¹⁹⁴ Even Staff witness Rearden admits that the peaking service had value.¹⁹⁵ Further, Staff witness Rearden's proposed adjustment is contrary to prior Commission precedent. In Docket No. 94-0040, the Commission held that only a portion of cost in excess of the amount deemed prudent should be disallowed, rather than disallowing all costs.¹⁹⁶ The Commission's rationale behind this decision was a concern that disallowing all costs could create an incentive for utilities to not undertake activities that are beneficial to customers.¹⁹⁷ In this docket, the Company reasonably believed that ratepayers would save money through the use of a bundled bid. The belief was borne out by the fact that Atmos had the lowest price of gas among Comparable Utilities under the 2005 Contract and the second lowest under the 2006 Contract.¹⁹⁸ There is no evidence in the record to support Staff witness Rearden's speculation that the Company should have issued RFPs for its system requirements in a piecemeal fashion. Certainly the Commission could not find that bidders would, in response to an unbundled RFP for peaking service, submit bids for free service. Accordingly, Staff's proposed adjustment should be rejected.

IV. CONCLUSION

The evidence in the record fully supports a finding that Atmos prudently procured its gas supply. The Company followed a competitive bidding process that complied with

¹⁹⁴ Company Ex. 4.0 at 23:475-478.

¹⁹⁵ Staff Ex. 4.0 at 11:224.

¹⁹⁶ *Ill. Commerce Comm'n v. Cent. Ill. Light Co.*, Docket No. 94-0040 (Order, Dec. 12, 1994).

¹⁹⁷ *See Id.* ("refusing to place at least a portion of CILCO's investment into rate base would likely cause companies who discover dangerous situation to put off renewal even longer and to attempt to continue repairing the system even when that approach is, perhaps, not the most economical solution.").

¹⁹⁸ Company Ex. 4.5; Company Ex. 4.6.

the Act and the Commission's rules, and Atmos selected the lowest bids available to it. Further, the price Atmos paid for gas was reasonable, competitive, and among the lowest price paid by Comparable Utilities. Accordingly, the Company respectfully requests that the Commission find Atmos prudently purchased gas for the 2006 reconciliation period and to reject Staff's proposed adjustments, with the exception of the accounting adjustments discussed in Section II.

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Respectfully submitted,

ATMOS ENERGY CORPORATION

By: /s/ _____
Patrick Huver
Attorney for Atmos Energy Corporation

Arthur Bresnahan
Patrick Huver
Zumpano, Patricios, Winker & Bresnahan, LLC
5202 Old Orchard Rd., Ste. 230
Skokie, IL 60077
(312) 924-3609
ab@zpwlaw.com
phuver@zpwlaw.com