

**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’S DRAFT ORDER

By the Commission:

I. 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 9-220 of the Public Utilities Act (the “Act”), (220 ILCS 5/1-101 et seq.), which directed Atmos Energy Corporation (“Atmos” or the “Company”) 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, 2006.¹

Notice of the filing of the Company’s direct testimony and exhibits was posted 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 Commission.² 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

¹ Initiating Order (Nov. 21, 2006).

² Tr. (May 1, 2012)

Commission.³ At the conclusion of the hearing on May 1, 2012 the record was marked "Heard and Taken."⁴

II. APPLICABLE AUTHORITY

In accordance with Section 9-220⁵ 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.⁶ 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." In each such proceeding, the burden of proof is on the utility to establish the prudence of its applicable costs.⁷

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 to be made.⁸ In determining whether a decision was prudently made, only those facts available at the time judgment was exercised can be considered. Hindsight review is impermissible in the context of a prudence determination.⁹

III. COMPANY'S INITIAL FILING

In accordance with the Commission's November 21, 2006 order in this proceeding, the Company made an initial filing on April 27, 2007.¹⁰ The Company's initial filing indicated total gas cost to be recovered under the PGA equal to \$15,953,366.09.¹¹ This consisted of gas costs equal to \$18,500,602.28, amounts

³ See Company Ex. 2.0-2.5; Company Ex. 3.0; Company Ex. 4.0 - 4.6; Staff Ex. 1.0 - 4.0.

⁴ Tr. at 88:5-8.

⁵ 220 ILCS 5/9-220.

⁶ *Id.*

⁷ *Id.*

⁸ *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); *Illinois Commerce Comm'n v. Commonwealth Edison Co.*, Ill. C.C. Docket No. 84-0395 (Order Date October 7, 1987, p. 17).

⁹ *Illinois Power Company v. Illinois Commerce Comm'n*, 245 Ill. App. 3d 365, 612 N.E. 2d 925, 929 (Ill. App. 1993); *Illinois Commerce Comm'n v. Commonwealth Edison Co.*, Ill. C.C. Docket No. 84-0395 (Order Date October 7, 1987, p. 17).

¹⁰ Company Ex. 1.0.

¹¹ *Id.* at 3:8-10; Company Ex. 1.1.

related to prior periods that represented an over-recovery equal to (\$2,426,038.49) and interest on unamortized balances equal to (\$121,197.70).¹²

In the course of the proceeding, Company witnesses provided testimony in support of its filing.¹³ As discussed below, Staff proposed certain adjustments to the Company's filing relating to particular issues but did not otherwise object to the amounts set forth in the Company's initial filing.

IV. UNCONTESTED ISSUES

A. Lost Gas

Ms. Everson proposed an adjustment for gas lost as a result of third party damage. Staff disagreed with the Company's practice of recording reimbursements as miscellaneous revenue.¹⁴ Instead, Ms. Everson recommended that reimbursements in the amount of \$2,350 be recorded as an offset to recoverable gas cost in the PGA.¹⁵ Mr. Martin testified that the Company has agreed to the adjustment for lost gas proposed by Ms. Everson.¹⁶ The Commission adopts Staff's proposed adjustment for lost gas.

B. NGPL Refunds

Ms. 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.¹⁷ Mr. Martin testified that the Company has agreed to the adjustment to include refunds from NGPL in its reconciliation.¹⁸ The Commission adopts Staff's proposed adjustment for NGPL refunds.

V. CONTESTED ISSUES

The contested issues in this docket are centered on the Company's gas supply contracts for its Harrisburg operating zone with Atmos Energy Marketing, a wholly owned affiliate of the Company ("AEM").¹⁹ The first contract was between the Company and AEM for the period of November 2005 through October 2006 ("2005 Contract").²⁰ The second contract was between the Company and AEM for the period of November

¹² Company Ex. 1.1.

¹³ Company Ex. 2.0-2.5; Company Ex. 3.0; Company Ex. 4.0-4.6.

¹⁴ Staff Ex. 1.0 at 3:37-43; Staff Ex. 1.0, Schedule 1.2.

¹⁵ *Id.*

¹⁶ Company Ex. 3.0 at 2:38-41.

¹⁷ Staff Ex. 1.0 at 3:45-50; Staff Ex. 1.0, Schedule 1.3.

¹⁸ Company Ex. 3.0 at 2:38-41.

¹⁹ Company Ex. 2.3-2.5.

²⁰ See Company Ex. 2.3-2.4 (2005 Contract).

2006 through October 2007 (“2006 Contract”).²¹ Staff witness Rearden has proposed adjustments related to (1) the price of baseload gas purchased under those contracts, and (2) the price of the peaking service under those contracts.²²

A. Baseload gas

Under both the 2005 Contract and the 2006 Contract, the price the Company paid for baseload gas was the East Texas TETCO price index (“ETX”) plus an additional amount above First of Month (“FOM”) ETX pursuant to Section 3.2 of the 2005 Contract and the 2006 Contract referred to by the parties as an adder (this amount is referred to as the “Adder” to protect confidentiality).²³ Staff witness Rearden alleged that the Company paid too high a price for gas.²⁴ Staff proposed an adjustment equal to the difference between the actual cost of gas paid by the Company and the cost if the Company had paid FOM ETX flat for all volumes, essentially disallowing the Adder.²⁵ The Company disagrees with Staff’s proposed adjustment.

1. Staff

Staff witness Rearden claimed that the Company paid an excessive price for baseload gas in 2006 and recommended an adjustment of (\$345,805).²⁶ Staff witness Rearden opined that in years immediately prior to the 2005 Contract and the 2006 Contract the Company paid a price of ETX-FOM flat, and argued that the inclusion of the Adder in the 2005 Contract and the 2006 Contract was an unreasonable price increase.²⁷ Staff witness Rearden testified that since there was only one bid for the 2005 Contract there is nothing to base a disallowance on besides the price agreed in the previous year.²⁸ Staff witness Rearden testified for the 2006 Contract there is nothing else in the record to base an alternative price on.²⁹ Staff witness Rearden opined that the Company should not have disqualified one of the nonconforming bids it received for the 2006 Contract, and speculated that this nonconforming bid could have been used to split the contract for Harrisburg supply with other suppliers.³⁰

²¹ See Company Ex. 2.3; Company Ex. 2.5 (2006 Contract).

²² Staff Ex. 3.0 at 11:224-12:231.

²³ Company Ex. 2.4 at § 3.2; Company Ex. 2.5 at § 3.2.

²⁴ Staff Ex. 3.0 at 11:224-228.

²⁵ *Id.*; Staff Ex. 3.0 at Schedule 3.1.

²⁶ Staff Ex. 3.0 at 2:41-44; Staff Ex. 3.0 at Schedule 3.1

²⁷ *Id.* at 5:73-79.

²⁸ Staff Ex. 4.0 at 10:210-217.

²⁹ *Id.*

³⁰ *Id.*

Staff witness Rearden opined that certain portions of the Company's request for proposals ("RFP") process may have discouraged bidders.³¹ Staff witness Rearden alleged that the Company required suppliers to affirmatively acknowledge that they wished to continue to receive RFPs.³² Staff witness Rearden opined that the Company could have stated that it would continue to issue RFPs unless a supplier requested otherwise.³³ Staff witness Rearden opined the requirement of affirmatively expressing interest made it less likely that a given supplier received an RFP the next year.³⁴ Staff witness Rearden opined that distributing more RFPs cannot result in lower bids and alleged that the cost to distribute additional RFPs was not likely to raise the total costs to ratepayers.³⁵ Staff witness Rearden also speculated that the Company might have generated more bids by accepting bids for less than the total supply.³⁶

Staff witness Rearden testified that the Company did not lease capacity on TETCO during the 2006 reconciliation period and therefore could not transport gas on its own account from the field to delivery points at Harrisburg and Galatia.³⁷ Staff witness Rearden noted that the Company previously had capacity on TETCO.³⁸ In 1996, Atmos' predecessor, United Cities Gas Company ("United Cities") held four TETCO firm transportation and storage contracts, two of which it assigned to Woodward Marketing, L.L.C. ("Woodward").³⁹ At the time, Woodward was controlled by J.D Woodward, with a minority interest held by United Cities.⁴⁰ Later, Atmos acquired United Cities.⁴¹ The Company stated that Atmos later indirectly acquired Woodward as a wholly owned subsidiary which became AEM.⁴²

Staff witness Rearden opined that this assignment of capacity made the market for gas supply to Harrisburg less competitive.⁴³ Staff witness Rearden opined that the transfer of capacity limited the competitive levels of the marketplace by eliminating the

³¹ Staff Ex. 3.0 at 7:132-8:145.

³² *Id.*

³³ *Id.*

³⁴ *Id.*

³⁵ Staff Ex. 4.0 at 9:183-188.

³⁶ *Id.* at 9:191-194.

³⁷ *Id.* at 5:82-90.

³⁸ Staff Ex. 3.0 at 582-90.

³⁹ Company Ex. 4.0 at 11:215-217.

⁴⁰ Company Ex. 3.0 at 7:141-144.

⁴¹ *Id.* at 7:139-146.

⁴² *Id.*

⁴³ Staff Ex. 3.0 at 5:92-6:107.

Company's direct access to the liquid downstream markets and by limiting the potential bidders to those suppliers that had capacity on TETCO.⁴⁴

As discussed in more detail later, the Company opined that United Cities' decision to rely on delivered service resulted in savings for its customers. Staff asserted that the Company did not provide evidence for this belief.⁴⁵ Staff witness Rearden testified that there are three reasons the Company's analysis on this point might be incorrect.⁴⁶ First Staff witness Rearden noted that the portfolio changed over time and the comparison may not mirror the options that the Company had in 2003.⁴⁷ Second, Staff witness Rearden noted the capacity was apparently allocated over several different customers and states, making it difficult to make a direct comparison.⁴⁸ Finally, Staff witness Rearden opined the value of transportation capacity may be greater than its cost.⁴⁹

2. Company

a. Gas Supply Contracts

The Company stated that the evidence in the record demonstrated no adjustment is necessary because the Company followed reasonable gas supply procurement procedures to award the 2005 Contract and the 2006 Contract.⁵⁰ Mr. Martin testified Company's gas procurement procedures comply with the Act and Commission rules and Staff has not disputed this.⁵¹ Mr. Martin testified that the Company uses competitive bidding to determine from whom it will purchase gas and the terms and conditions that will apply to the purchase.⁵² Mr. Martin noted that the Company solicits bids through a RFP, obtains bids from vendors, analyzes each bid and determines which conforming bid is the best offer for the Company and customers.⁵³ The Company noted that it is undisputed that the Company selected what it expected to be the lowest bid of the two bids it analyzed.⁵⁴

⁴⁴ *Id.* at 6:110-117.

⁴⁵ Staff Ex. 4.0 at 5:100-107.

⁴⁶ *Id.* at 6:109-7:138.

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ Company Ex. 2.0 at 3:56-5:95.

⁵¹ See *Id.* at 15:316-318 (procedures comply with the Act and Commission rules).

⁵² *Id.* at 3:56-57

⁵³ *Id.* at 5:88-90.

⁵⁴ See Company Initial Brief at § III; Company Ex. 4.0 (describing analysis of bids); Company Ex. 4.2 (Original RFP analysis); Company Ex. 4.3 (revised RFP analysis).

The Company showed that it received three bids in the 2006 RFP, 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.⁵⁵ Mr. Martin testified that the only fully conforming bid was AEM's proposal.⁵⁶ A second proposal was essentially non-conforming because it failed to quote the preferred price index specified in the RFP, Platt's Inside FERC Gas Market Report ("IFGMR") ETX.⁵⁷ The Company stated the second bid proposed the alternate index point IFGMR Texas Eastern M3.⁵⁸ This bidder is referred to as the "M3 Supplier" to protect confidentiality. Mr. Martin testified 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 alternate index point.⁵⁹ Mr. Martin testified that to facilitate analysis of the competitive bids, the M3 Supplier's proposal was considered for further evaluation along with the fully conforming bid.⁶⁰

Mr. Martin testified that 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.⁶¹ Mr. Martin testified that because of the nonconforming bid, the M3 Supplier's proposal had to be evaluated using the historical pricing of the alternate index.⁶² 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 2006.⁶³ The Company asserted this review revealed that the ETX index price was lower than the M3 index price in every historic month of the period examined.⁶⁴ Mr. Martin testified 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.⁶⁵

Mr. Martin testified that a subsequent review of the annualized cost comparison revealed a calculation error.⁶⁶ The Company stated the correction of this error would not have changed the Company's analysis because the revised analysis estimated an even

⁵⁵ Company Ex. 3.0 at 230-231; Company Ex. 4.0 at 13:260-266.

⁵⁶ Company Ex. 4.0 at 13:262-263.

⁵⁷ *Id.* at 14:266-14:268.

⁵⁸ *Id.* at 14:276-280.

⁵⁹ *Id.* at 14:269-275.

⁶⁰ *Id.* at 14:276-280.

⁶¹ *Id.* at 14:281-285; Company Ex. 4.2.

⁶² *Id.* at 14:276-280.

⁶³ Company Ex. 4.0 at 17:342-344.

⁶⁴ *Id.* at 17:344-347.

⁶⁵ *Id.*; Company Ex. 4.0 at 15:313-316.

⁶⁶ Company Ex. 4.0 at 16:323-335.

greater savings with AEM's bid.⁶⁷ Mr. Martin testified that the corrected annualized cost comparison estimated that AEM's proposal would result in savings of more than \$500,000 in comparison to the M3 Supplier's proposal.⁶⁸

Mr. Martin testified that the Company received one bid for the 2005 Contract.⁶⁹ Mr. Martin testified that the protections of competitive bidding remained in place for the 2005 Contract because AEM could not assume that it would be the only bidder, as evidenced by the two additional bids received for the 2006 Contract (one of which was nonconforming).⁷⁰ The Company asserted that it was aware that the price of the bid was higher than in prior years.⁷¹ However, the Company understood that the market was in disarray as a result of two catastrophic hurricanes causing extensive damage in the Gulf of Mexico.⁷² 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.⁷³ The Company asserted that it had substantial reasons to find it prudent to enter into the 2005 Contract, including its knowledge of the gas supply market.⁷⁴ The Company stated that it believed the price of the 2005 Contract was reasonable, given its understanding of the market conditions.⁷⁵

The Company stated that the evidence in record does not support Staff witness Rearden's proposed adjustment to the cost of baseload gas.⁷⁶ The Company argued that Staff witness Rearden has admitted he reached his conclusion that the Company paid too high a cost for baseload gas without providing any evidence of what a reasonable price increase would be.⁷⁷ The Company stated that this price was not available in the marketplace to it as evidenced by its own RFPs, its knowledge of the market, and the fact that three other Illinois utilities served by TETCO and identified by Staff as comparable to the Company (the "Comparable Utilities") all entered into contracts charging significantly higher prices for baseload gas during this period.⁷⁸ Mr. Martin testified that the Company would have selected ETX flat if it were available.⁷⁹

⁶⁷ *Id.*

⁶⁸ *Id.*

⁶⁹ Company Ex. 2.0 at 5:103-106.

⁷⁰ Company Ex. 4.0 at 22:452-459.

⁷¹ Company Initial Brief at § III.B.2.

⁷² Tr. at 33:1-34:5.

⁷³ Tr. at 58:7-13.

⁷⁴ Company Ex. 2.0 at 9:181-10:193; Tr. at 58:7-13.

⁷⁵ *Id.*

⁷⁶ Company Initial Brief at § III.C.1

⁷⁷ Tr. at 81:16-19.

⁷⁸ Company Ex. 3.0 at 13:257-263.; Company Ex. 4.0 at 20:406-410.

⁷⁹ Company Ex. 3.0 at 13:257-258.

The Company stated that Staff's adjustment attempts to unreasonably impose a prudence baseline that was not available in the marketplace.⁸⁰

The Company stated that the availability of a price at one point in time does not mean that price will continue to be available in the future.⁸¹ The Company noted that Staff witness Rearden has admitted that, in general, he believes gas prices change over time.⁸² The Company presented evidence that the gas marketplace was experiencing severe volatility during the period in question.⁸³ Mr. Martin testified that at the time the RFPs were issued, the marketplace was in disarray.⁸⁴ Specifically, Mr. Martin testified that a major hurricane in the Gulf of Mexico called Hurricane Katrina caused extensive damage to offshore gas platforms.⁸⁵ Mr. Martin testified that shortly thereafter, the Gulf of Mexico was again disrupted by Hurricane Rita.⁸⁶

The Company noted that Staff witness Rearden appears to suggest that utilities can obtain gas at flat index prices.⁸⁷ Yet, the Company argues, Staff witness Rearden admitted that utilities commonly enter into contracts with suppliers with adjustments (adders or discounts) to the index price.⁸⁸ Mr. Martin 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.⁸⁹ Mr. Martin testified that because the volatility in the market place due to Hurricane Katrina and Hurricane Rita, forward prices for ETX were trading at a significant discount to Louisiana and New York Mercantile Exchange ("NYMEX") related prices.⁹⁰ The Company stated that based on its market knowledge, the Company determined that entering into a contract with a price of ETX plus the Adder was a prudent decision.⁹¹ The Company opined that Staff's price adjustment based on FOM ETX flat is unreasonable in light of the strong evidence presented by the Company that the marketplace was experiencing severe volatility.⁹²

⁸⁰ Company Initial Brief at III.C.1; See Company Ex. 3.0 at 13:257-14:280.

⁸¹ Company Ex. 3.0 at 13:257-363.

⁸² Tr. at 82:4-6.

⁸³ Company Ex. 2.0 at 9:181-187.

⁸⁴ *Id.*; Tr. at 33:7-17.

⁸⁵ Tr. at 33:7-22.

⁸⁶ *Id.*

⁸⁷ Staff Ex. 3.0 at 5:73-78; *Id.* at 11:218-221; Tr. at 83:22-84:5.

⁸⁸ Tr. at 84:6-15.

⁸⁹ *Id.* at 60:21-61:7.

⁹⁰ Company Ex. 2.0 at 9:181-10:199.

⁹¹ *Id.*

⁹² Company Initial Brief at § III.C.1; Company Ex. 2.0 at 9:181-10:193; Tr. at 58:7-13.

The Company opines that Staff's argument 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.⁹³ Mr. Martin explained that often which index and adder is used is not truly important other than as a means to compare market pricing.⁹⁴ The Company used its knowledge of the marketplace to prudently determine that the 2005 Contract and 2006 offered reasonable pricing.⁹⁵ The Company stated that prudence of this view was confirmed through examination of the pricing paid by Comparable Utilities.⁹⁶ The Company noted that despite the fact that the 2005 Contract and the 2006 Contract had a higher Adder than the Comparable Utilities, Atmos actually paid the lowest price for gas of the Comparable Utilities under the 2005 Contract and the second lowest under the 2006 Contract.⁹⁷ The Company opined that this highlights the need to focus on the index in addition to the adder. The Company stated that although there is no Commission requirement to obtain the lowest pricing of all other utilities, the fact that the Company did demonstrates the pricing it obtained was reasonable.⁹⁸

b. Alternate Price

The Company disagrees with the suggestion by Staff that there is no alternate price to base the prudence of the contracts on.⁹⁹ Mr. Martin testified that the Company can award a gas supply contract to AEM only if AEM submits the lowest bid.¹⁰⁰ The Company stated that the fair market price is established by the market composed of willing buyers and sellers.¹⁰¹ For the 2006 reconciliation period, the Company stated that the fair market resulted from the RFP process undertaken by the Company to determine the least cost bid for gas supply in its five operating zones.¹⁰² The Company stated that AEM submitted the lowest bids for one of these operating zones, Harrisburg.¹⁰³ Mr. Martin testified that 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.¹⁰⁴ However, the Company noted that in the Harrisburg operating zone in

⁹³ See Company Ex. 4.0 at 4:77-82.

⁹⁴ Company Ex. 2.0 at 9:172-180.

⁹⁵ Company Ex. 2.0 at 9:181-10:193.

⁹⁶ Company Initial Brief at § III.B – III.C; See Company Ex. 4.0 at 20:410-22:445. Company Ex. 4.5; Company Ex. 4.6.

⁹⁷ See Company Ex. 4.5; Company Ex. 4.6.

⁹⁸ See Company Ex. 4.0 at 22:460-466.

⁹⁹ *Id.* at 22:442-451.

¹⁰⁰ *Id.* at 22:442-443.

¹⁰¹ *Id.* at 22:443-444.

¹⁰² *Id.* at 22:444-446.

¹⁰³ *Id.* at 22:446-47.

¹⁰⁴ *Id.* at 22:447-449.

which AEM submitted the lowest bid, Staff claims it is unable to determine the real fair market price.¹⁰⁵

The Company stated that the Comparable Utilities pricing data presents an additional basis for determining an alternate price. The Company presented evidence that it paid the lowest price of gas among the Comparable Utilities under the 2005 Contract and the second lowest under the 2006 Contract.¹⁰⁶ Mr. Martin testified that although the Company is not required to obtain the lowest pricing of all other utilities, the fact that the Company did is another basis for determining the pricing was reasonable.¹⁰⁷ Mr. Martin testified that the evidence in the record demonstrates that not only was there an alternate price, that the alternate price was significantly higher than the price paid by the Company for gas.

c. RFP Procedures

Staff witness Rearden opined that the Company reduced the number of potential bidders by requiring suppliers to affirm that they wished to continue to receive RFPs.¹⁰⁸ The Company stated that Staff witness Rearden's opinion is not supported by the record. The Company noted that even Staff witness Rearden admitted it was unknowable whether more bids would have been received if the Company had used an affirmative option instead of a negative option.¹⁰⁹

Atmos noted that Staff appeared to be confused about the Company's RFP procedures, and clarified that the Company's procedures merely removed the entities least interested in bidding by removing entities on the mailing list that had never bid and failed to state their interest in ever doing so.¹¹⁰ Staff witness Rearden claimed removing entities from the mailing list resulted in fewer bidders over time starting with 2003.¹¹¹ The Company stated that the facts show that Staff witness Rearden's assertion is incorrect. The Company noted that it received more bids in the 2006 RFP (three) than it did in the 2003 RFP (two) and the 2004 RFP (one).¹¹² The Company noted that Staff considers the price obtained by the 2004 RFP to be prudent and alleges that the price obtained by the 2006 RFP is imprudent.¹¹³

¹⁰⁵ *Id.* at 22:449-451.

¹⁰⁶ See Company Ex. 4.5; Company Ex. 4.6.

¹⁰⁷ See Company Ex. 4.0 at 22:460-466.

¹⁰⁸ Staff Ex. 3.0 at 7:132-8:145.

¹⁰⁹ Company Ex. 4.0 at 6:104-160; Staff Ex. 4.0 at 9:180-183.

¹¹⁰ *Id.* at 6:108-114.

¹¹¹ Staff Ex. 4.0 at 8:166-167; Tr. at 80:3-80:20.

¹¹² Company Ex. 4.0 at 6:115-120; See Staff Ex. 3.0 at 7:137-8:140.

¹¹³ Staff Ex. 3.0 at 5:73-79.

Staff witness Rearden additionally complained that the Company should not have rejected the nonconforming bid.¹¹⁴ Mr. Martin testified to several reasons why the Company could not accept the nonconforming bid.¹¹⁵ First, the Company stated that it 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.¹¹⁶ Second, the nonconforming bid only represented a fraction of the baseload requirement in the RFP, and none of the peaking requirement.¹¹⁷ The Company stated that it 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.¹¹⁸ Third, Mr. Martin testified the Company solicits RFPs for full system requirements because the Company believes this will yield better pricing through economies of scale than through piecemeal solicitation.¹¹⁹ Fourth, Mr. Martin testified the Company believes bidders will be less likely to bid or bid a higher price on RFPs with open-ended terms than with specific terms.¹²⁰

d. Delivered Service

Staff witness Rearden opined that the Company's use of delivered service instead of having transportation capacity was imprudent.¹²¹ The Company noted that Staff witness Rearden conceded that neither delivered service or transported service is always low cost.¹²² The Company presented evidence that in its opinion showed the decision to rely on delivered service actually saved the customers money.¹²³ The Company filed a comparison between the supplier demand charges from November 2003 through December 2006 to the demand charges Atmos would have paid to hold the same necessary pipeline capacity on TETCO.¹²⁴ Mr. Martin testified this analysis showed a savings in excess of one million dollars.¹²⁵ Mr. Martin testified that he believed there would be similar savings both prior to and after that period.¹²⁶

¹¹⁴ *Id.* at 9:166-174.

¹¹⁵ Company Ex. 4.0 at 19:387-20:409.

¹¹⁶ Company Ex. 4.0 at 19:387-391.

¹¹⁷ *Id.* at 19:392-399.

¹¹⁸ *Id.*

¹¹⁹ *Id.* at 19:400-409.

¹²⁰ *Id.*

¹²¹ Staff Ex. 3.0 at 5:80-6:107.

¹²² Staff Ex. 4.0 at 4:80-81.

¹²³ Company Ex. 4.0 at 10:184-200; Company Ex. 4.1.

¹²⁴ *Id.*

¹²⁵ *Id.*

¹²⁶ Company Ex. 4.0 at 10:197-200.

The Company noted that 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 with a good degree of certainty.¹²⁷ The Company stated that Staff witness Rearden correctly points out that each approach has pros and cons that may outweigh cost savings.¹²⁸ The Company pointed out that prudence standard recognizes that reasonable minds can disagree.¹²⁹ The Company stated that because neither delivered service or transport capacity is clearly better, the Company's decisions to rely on delivered service cannot be found imprudent, especially when the Company reasonably believed it could be less expensive.¹³⁰

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.¹³¹ The Company disagreed and stated that 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.¹³² The Company stated that Staff's suggestion to consider the costs of one year without acknowledging any potential benefits is cherry-picking.¹³³ Mr. Martin testified that this assumes there is a cherry to pick.¹³⁴ As previously discussed, the Company argued that its 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.¹³⁵

e. TETCO Capacity Release

Staff witness Rearden alleges that Atmos' predecessor was imprudent to release capacity on TETCO. Mr. Martin testified that more than fourteen years ago, before Atmos was operating in Illinois, its predecessor, United Cities held four TETCO firm transportation and storage contracts.¹³⁶ Mr. Martin testified that in 1996, United Cities made a decision to release its transportation capacity and instead take delivered

¹²⁷ See Staff Ex. 4.0 at 6:109-7:138; Company Ex. 4.0 at 8:159-162.

¹²⁸ Company Ex. 4.0 at 8:162-9:167.

¹²⁹ *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.'").

¹³⁰ Company Ex. 4.0 at 8:162-9:167.

¹³¹ Staff Ex. 4.0 at 5:88-90.

¹³² See *Ill. Commerce Comm'n v. Ill. Power Co.*, Docket No. 01-0701 at 7 (Order, Feb. 19, 2004).

¹³³ Company Ex. 3.0 at 8:161-168.

¹³⁴ *Id.*

¹³⁵ See Company Ex. 4.5; 4.6.

¹³⁶ Company Ex. 4.0 at 11:215-217.

service.¹³⁷ Mr. Martin testified that starting in September 1996, two of the transportation contracts were terminated and Woodward did not obtain this released capacity.¹³⁸ The Company noted that Woodward did obtain the interstate pipeline capacity released by United Cities to TETCO under the other two contracts.¹³⁹

Staff witness Rearden alleges that not holding transportation capacity resulted in Atmos' RFP process becoming monopolized by AEM.¹⁴⁰ The Company stated that 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 2004-2008.¹⁴¹ Mr. Martin testified that the number of times AEM submitted winning bids was comparable to the number of times non-affiliates submitted winning bids.¹⁴² In addition, the Company submitted evidence that Atmos has obtained gas supply from twelve different suppliers on TETCO between November 1997 through 2006.¹⁴³ The Company opined that the wide variety of different suppliers demonstrates that Atmos' RFP process has not been dominated by one entity.

More importantly, the Company noted that 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.¹⁴⁴ Atmos noted that the Commission has found the prices the Company has paid for gas to be reasonable in the decade leading up to November 2005.¹⁴⁵ The Company opined that Staff witness Rearden's speculation on this issue relies on an assumption that the Company received fewer bids over time.¹⁴⁶ The Company stated this assumption is ungrounded because the number of bids actually increased during the 2006 RFP in comparison to prior years.¹⁴⁷ Additionally, the Company noted that the bidding entities had no knowledge of the number of bids the Company was receiving.¹⁴⁸ The Company opined that the bidding entities could not bid a very high price as suggested by Staff witness Rearden because the bidding entity would risk losing the contract.¹⁴⁹ The Company pointed out

¹³⁷ *Id.* at 11:220-221.

¹³⁸ *Id.* at 11: 217-218.

¹³⁹ *Id.* at 11:218-222.

¹⁴⁰ Staff Ex. 3.0 at 8:155-160.

¹⁴¹ Company Ex. 4.0 at 12:229-244.

¹⁴² *Id.*

¹⁴³ Company Ex. 2.2.

¹⁴⁴ Staff Ex. 4.0 at 8:162.

¹⁴⁵ Company Ex. 3.0 at 8:147-153.

¹⁴⁶ See Staff Ex. 4.0 at 8:162-170.

¹⁴⁷ Company Ex. 4.0 at 6:115-120.

¹⁴⁸ *Id.* at 9:172-175.

¹⁴⁹ *Id.* at 9:175.

that 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.¹⁵⁰

The Company argues that Staff's review of the capacity release in this proceeding is inappropriate in this docket. The Company stated that 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.¹⁵¹

3. Commission Analysis and Conclusion

The Commission finds that the evidence in the record demonstrates that Atmos prudently entered into gas supply contracts with AEM for 2006. Although the Commission agrees with Staff that transactions with affiliates warrant extra scrutiny, the Company's RFPs appear to have been conducted in accordance with all applicable law. Although particular procedures may always be refined and modified in an effort to improve bidding, no party has raised any fundamental issues with respect to the Company's process. The Commission is satisfied that Atmos obtained a reasonable and competitive price under the 2005 Contract and the 2006 Contract.

Therefore, the Commission declines to adopt the adjustment proposed by Staff. The Commission notes that the natural gas market is not static, and the marketplace during the period in question was experiencing severe volatility. Because of this volatility, the Commission finds that the price obtained in a prior year's contract is not a reliable indicator of the pricing available in 2006. The Commission notes that in addition to observing an RFP process that complied with applicable Commission requirements, the Company relied on its knowledge of the market and generally available pricing to assess the reasonableness of the bids. The Commission notes that the Company had a reasonable basis to believe the price of gas it obtained was competitive. While we do not impose any kind of test comparing one utilities' prices to another (or consider such a comparison in any way dispositive), we find it unlikely that a utility that obtained among the lowest pricing of a group of Comparable Utilities would be the one utility that had acted imprudently in acquiring gas supply.

B. Peaking

As part of the Company's gas supply procurement process, the Company forecasted that it would 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 period.¹⁵² The option to take the additional 2900 dekatherms on ten days during the winter period

¹⁵⁰ Company Ex. 4.5; Company Ex. 4.6.

¹⁵¹ Company Ex. 3.0 at 9:169-174.

¹⁵² Company Ex. 2.0 at 14:293-306.

is referred to as peaking service and is a common way to address the fact that demand for natural gas depends on unpredictable weather.¹⁵³

1. Staff

Staff witness Rearden alleged the Company paid an excessive price for peaking service and recommended a disallowance of the entire cost of the peaking service.¹⁵⁴ Staff witness Rearden noted the Company bundled peaking service with baseload and incremental volume purchases, and alleged that the Company relied on the outcome of bundled contracts to justify overpriced peaking service.¹⁵⁵

Staff witness Rearden testified that the demand charge per Dth Atmos paid for peaking equaled the demand charge per Dth that Atmos paid for baseload demand.¹⁵⁶ Staff witness Rearden testified that Atmos paid the same for a service in which Atmos could take delivery for only ten days during a five-month period as it could have for a service in which Atmos could take delivery every day of the year.¹⁵⁷ Staff witness Rearden opined that Atmos was not able to independently generate a value for the peaking service because it did not put the service out for bid separately from its overall gas supply requirements.¹⁵⁸ Therefore, Staff recommended a disallowance of the entire cost of the peaking service.

2. Company

The Company noted that no party disputed the need for the peaking service or that its customers benefitted from the service that the Company acquired under the 2005 Contract and the 2006 Contract. The Company asserted that Staff witness Rearden's proposed adjustment is not supported by the record or Commission precedent.¹⁵⁹

The Company asserted that it prudently incurred the costs of the peaking service, and therefore Staff's proposed adjustment is unjustified.¹⁶⁰ The Company noted that 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 Commission rules.¹⁶¹ The Company analyzed the bids it

¹⁵³ *Id.*

¹⁵⁴ Staff Ex. 1.0 at Schedule 1.5; Staff Ex. 3.0 at 14:272-291.

¹⁵⁵ *Id.*

¹⁵⁶ *Id.* at 14:279-291.

¹⁵⁷ Staff Ex. 3.0 at 14:279-291.

¹⁵⁸ Staff Ex. 4.0 at 11:231-234.

¹⁵⁹ See Company Initial brief at § III.C.2

¹⁶⁰ Company Ex. 4.0 at 23:479-493.

¹⁶¹ Company Ex. 2.0 at 15:316-318.

received and selected the bid it believed to represent the lowest bid as a whole.¹⁶² For the 2006 RFP, the other qualifying bidder priced its peaking service somewhat lower than AEM.¹⁶³ Atmos asserted that it took this into consideration when evaluating the bids, but because AEM had significantly lower baseload gas pricing, the difference was not significant enough to make the overall contract more favorable to the Company.¹⁶⁴ Mr. Martin testified that as a whole, the AEM offer was better.¹⁶⁵ The Company asserted that Staff did not disagree with the Company's analysis of the bids or the determination that AEM was the overall low bidder.¹⁶⁶

The Company also disputed Staff's claim that the Company should not have bundled bids for peaking service with other system requirements. The Company asserts that 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.¹⁶⁷ The Company noted that the Commission recognizes that reasonable minds can differ and still be prudent.¹⁶⁸ The Company asserts that it had a reasonable basis for believing bundling the system requirements would result in a lower overall price.¹⁶⁹ The Company reiterated that at the time it believed RFPs for full system requirements would yield better pricing through economies of scale than through piecemeal solicitation.¹⁷⁰

In addition, the Company asserted that Staff's complete disallowance of costs was contrary to the record. Mr. Martin testified that as much as the Company would like to pay lower prices for any service, it will never be able to obtain peaking service for free.¹⁷¹ The Company noted that even Staff witness Rearden admits that the peaking service had value.¹⁷²

The Company further asserted that Staff witness Rearden's proposed adjustment is inconsistent with prior Commission precedent.¹⁷³ The Company noted that in Docket

¹⁶² *Id.* at 15:318-320.

¹⁶³ Company Ex. 3.0 at 14:290-295.

¹⁶⁴ *Id.*

¹⁶⁵ *Id.*

¹⁶⁶ Company Initial Brief at § III.B.2

¹⁶⁷ Company Initial Brief at § III.C; see Tr:77:4-78:5.

¹⁶⁸ 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.'");

¹⁶⁹ Company Ex. 4.0 at 19:387-20:409.

¹⁷⁰ *Id.* at 19:400-409.

¹⁷¹ *Id.* at 23:475-478.

¹⁷² Staff Ex. 4.0 at 11:224.

¹⁷³ Company Initial Brief at § III.C.2

No. 94-0040, the Commission held that only portion of cost in excess of the amount deemed prudent should be disallowed, rather than disallowing all costs.¹⁷⁴ The Company described the Commission's rationale behind this decision as a concern that disallowing all costs could create an incentive for utilities to not undertake activities that are beneficial to customers.¹⁷⁵ In this docket, the Company asserted that it reasonably believed that ratepayers would save money through the use of a bundled bid. The Company asserts that this belief was confirmed 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.¹⁷⁶

3. Commission Analysis and Conclusion

The Commission finds that the evidence in the records demonstrates that Atmos prudently entered into peaking arrangements for the 2006 reconciliation period. The Commission notes that Atmos engaged in a competitive bidding process that complied with the Commission's rules and selected the lowest overall bids available. The Commission is satisfied that Atmos obtained the lowest price available when considering the bids as a whole. The Commission further notes that it is undisputed the peaking service had value. Therefore, the Commission declines to adopt the adjustment to the price of peaking proposed by Staff.

Accordingly the Commission finds that Atmos had total cumulative gas recoveries of \$15,950,641.39 and total gas recoveries of \$17,104,998.29 resulting in a combined over recovery of (\$1,154,356.90). Of this amount, \$1,151,631.90 has been refunded through monthly PGA filings. Therefore, \$2,725 is to be refunded to customers through Factor O.

VI. FINDINGS AND ORDERING PARAGRAPHS

The Commission, having given due consideration to the entire record herein, is of the opinion and finds that:

- (1) Atmos is a corporation engaged in the distribution of natural gas service to the public in portions of the State of Illinois and, as such, is a public utility within the meaning of the Act;
- (2) the Commission has jurisdiction over Atmos and of the subject matter of this proceeding;

¹⁷⁴ *Ill. Commerce Comm'n v. Cent. Ill. Light Co.*, Docket No. 94-0040 (Order, Dec. 12, 1994).

¹⁷⁵ *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.").

¹⁷⁶ Company Ex. 4.5; Company Ex. 4.6.

- (3) the statements of fact set forth in the prefatory portion of this Order are supported by evidence of record and are hereby adopted as finding of fact;
- (4) the approved reconciliation of revenues collected under Atmos' PGA with the actual cost of gas supplies during the reconciliation period, as described in the Appendix attached hereto, should be accepted.
- (5) Atmos should implement Factor O refunds of \$2,725 in its first monthly Gas Charge filing after the date of this Order.

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that the reconciliation of costs actually incurred for the purchase of gas with the revenue received for such gas by Atmos for calendar year 2006, as set forth in the Appendix hereto, is approved.

IT IS FURTHER ORDERED that subject to the provisions of Section 10-113 of the Act and 83 Ill. Adm. Code 200.880, this Order is final; it is not subject the Administrative Review Law.