

AGENDA INFORMATION SHEET
AGENDA ITEM NO. _____

**APPROVAL OF A CHANGE IN ATMOS ENERGY CORPORATION,
MID-TEX DIVISION'S ("ATMOS") RATES AS A RESULT OF
SETTLEMENT BETWEEN ATMOS AND THE ATMOS TEXAS
MUNICIPALITIES ("ATM") UNDER THE RATE REVIEW
MECHANISM FOR 2015**

ATMOS TEXAS MUNICIPALITIES

The City is a member of the Atmos Texas Municipalities (ATM). The ATM group was organized by a number of municipalities served by Atmos and has been represented by the law firm of Herrera & Boyle, PLLC (through Mr. Alfred R. Herrera). ATM also retained the services of a consulting firm, Utilitech, Inc. (Mr. Mike Brosch and Mr. Steve Carver) to assist in reviewing an application submitted by the Atmos Energy-Mid-Tex Division (Atmos) that seeks to increase its rates and change its rates. Herrera & Boyle, PLLC and Utilitech, Inc. have participated in prior rate cases involving Atmos and have extensive knowledge and experience in rate matters affecting Atmos' rates, operations, and services.

HISTORY OF PRIOR RATE INCREASES

Increase Under Previous Version of RRM (Approved October 2010)

On March 15, 2010, Atmos requested an increase of \$70.1 million in its system-wide rates. ATM and Atmos settled on an increase of \$27 million for prospective rates.

Increase Under Previous Version of RRM (Approved September 2011)

On April 1, 2011, Atmos filed a request to increase rates system-wide by \$15.6 million. ATM and Atmos agreed to not increase base rates and permitted Atmos to recover \$6.6 million for the steel pipe replacement program.

General Rate Case (Approved December 2012)

In January 2012, Atmos sought an increase of about \$49.1 million. Ultimately, the ATM cities and Atmos were not able to reach agreement on an increase and Atmos filed an appeal to the Railroad Commission of Texas. The Railroad Commission approved an increase of about \$24.1 million, representing an increase in revenue of about 7%.

Increase Under Current RRM (July 2013)

In the summer of 2013, Atmos and ATM entered into an agreement that approved a revised Rate Review Mechanism (RRM). The RRM approved in the summer of 2013 is the third iteration of that rate-setting mechanism.

On about July 15, 2013, Atmos submitted a request to increase rates under the current RRM. Atmos requested an increase in rates on a system-wide basis of \$22.7 million, which is an increase of about 5%. Following a series of settlement negotiations between Atmos' experts and ATM's experts, Atmos agreed to an increase of \$16.6 million, an increase in revenue of about 3.7%.

Prior Increase Under the RRM (June 2014) – Atmos Filed Appeal With the Railroad Commission – Gas Utility Docket (GUD) No. 10359:

On about February 28, 2014, Atmos filed its second request to increase rates under the current iteration of the RRM (the "2014 RRM") and requested a system-wide increase of about \$45.6 million (9.2% increase in revenue). ATM's consultants' preliminary assessment indicated that Atmos warranted at most an increase of \$26.6 million. A settlement was not reached, the ATM cities denied Atmos' proposed increase, and Atmos appealed ATM's denial of its revenue increase to the Railroad Commission. On appeal Atmos revised its request downward from \$45.6 million to \$43.8 million. Atmos implemented the full rates on June 1, 2014, subject to refund. The Commission held a hearing on September 3, 2014, and did not issue the hearing examiner's proposal for decision ("PFD") until last week on April 28, 2015. The hearing examiner proposed an increase of \$42.9 million, that is, only about \$860,000 less than Atmos requested.

2015 RRM APPLICATION UNDER THE CURRENT RATE REVIEW MECHANISM

On February 27, 2015, Atmos submitted an application under the current RRM seeking a *system-wide* rate increase of \$28.7 million ("2015 RRM"), which equates to an increase of about 5.6%. After review of Atmos' application, and of the Railroad Commission's proposal for decision in GUD No. 10359 (as is explained in more detail below), ATM's Special Counsel and ATM's consultant, Utilitech, Inc., concluded Atmos merited an increase of no more than about \$9.1 million ("Report"). However, ATM's consultants completed that report without the benefit of the Commission's PFD for the 2014 RRM. ATM's Special Counsel and consultants had hoped to have direction from the Commission on many of the disputes that arose in the 2014 RRM resolved so as to inform their analysis of Atmos' 2015 RRM. If the Commission adopts the PFD for the 2014 RRM, which is the most likely scenario, many of the recommendations supported by ATM will be eliminated or modified. Therefore, ATM's Special Counsel and consultants' preliminary findings of a \$9.1 million increase, would have to be adjusted to accommodate the PFD issued in the 2014 RRM and would produce an increase closer to about \$23 million.

At this juncture, the ATM cities' options are as follows:

Option 1. To deny Atmos' requested increase under the 2015 RRM and approve no increase;

Option 2. To deny Atmos' requested increase and approve an increase of no more than \$9.1 million for its 2015 RRM, based on ATM's consultants' preliminary report;

Option 3. To take no action and allow Atmos' proposed increase of \$23.9 million in the affected cities and its related rates to go into effect; or

NOTE: *If the City elects Option 1, Option 2, or Option 3, the City would also have to continue its participation in the appeal pending at the Railroad Commission in GUD No. 10359 and incur its attendant costs.*

Option 4. To approve a settlement agreement that resolves the 2014 RRM and the 2015 RRM, which combined results in an increase in rates above 2013 revenues of \$65.7 million.

Note that under Option 1 and Option 2, Atmos has the right to appeal the ATM cities' decisions to the Railroad Commission of Texas and pending such an appeal has the right to implement its proposed increase of \$23.9 million effective June 1, 2015, subject to refund if the Commission's review later finds a lower amount is appropriate. Atmos has notified ATM's Special Counsel of Atmos' intent to file an appeal of the City's decision to deny its requested increase.

In an appeal to the Commission, Atmos would in all likelihood argue that the costs of appeal should be borne by only the ATM cities. Given the Commission's tendency to err in favor of utilities, Atmos would likely prevail. An appeal would increase the burden on ratepayers by adding rate case expenses, which would include both ATM's and Atmos' costs of preparing and prosecuting the appeal, and the costs of a hearing.

RECOMMENDATION:

After a series of negotiations with Atmos, and given the significant downside of continued litigation of this matter, ATM's Special Counsel recommends resolving both the 2014 RRM and 2015 RRM in a single settlement agreement. Continued efforts at the Commission with regard to the 2014 RRM will result in more rate case expenses and are unlikely to result in any material changes to the PFD in favor of ATM. Also, because the Commission issued the PFD regarding the 2014 RRM at such a late date, it undermined ATM's consultants' ability to incorporate the proposed decisions regarding the 2014 RRM, into their 2015 RRM report.

If the ATM rejects Atmos' settlement offer, Atmos would appeal the cities' decision to the Railroad Commission. While there are a number of contested issues whose outcome are uncertain in an appeal, based on the Proposal for Decision regarding Atmos' 2014 RRM, ATM's Special Counsel and consultants are of the opinion that the Railroad

Commission would reach the same results its hearing examiner reached in regarding the 2014 RRM. That is, the probability is high that on appeal the Railroad Commission would award Atmos all or most of its 2015 RRM request, \$23.9 million, as well as \$42.9 million of its 2014 RRM request. At part of the settlement of Atmos' 2014 *and* 2015 RRMs, Atmos will dismiss its appeal of the 2014 RRM and will not seek recovery of RRM rate case expenses.

Therefore, because of the risks of an unfavorable outcome at the Railroad Commission, ATM's special counsel advises the ATM cities to accept a settlement increasing rates by about \$21.87 million over the current, interim rates Atmos is charging. Because the current rates Atmos is charging have not been approved by either the cities or the Railroad Commission, the City's action in effect would be to approve an increase for the 2014 RRM filing *and* the 2015 RRM filing of about \$65.7 million, combined, over Atmos' 2013 proposed revenues. The Settlement Agreement is appended as "Attachment A."

The combined increases for the 2014 RRM and 2015 RRM are shown below:

2014 RRM	
System Wide	
2014 RRM Filed City Amount	\$45,732,838
Adjustments	(1,913,950)
2014 RRM Filed Appeal Amount	<u>43,818,888</u>
Adjustments:	
CC 1205	(27,748)
AtmoSpirit and Service Awards	(196,741)
Depreciation on Disallowed Projects	(349,906)
Incentive Compensation to Achieved payout of 150%	(84,555)
Flow Through effect of incentive adjustment	(6)
ADIT NOL Correction	(36,545)
Other Revenue: Forfeited Discount	(122,668)
Flow through effects of above adjustments	(42,088)
PFD Amount	<u>\$42,958,631</u>
2015 RRM	
System Wide	
2015 RRM Filed City Amount (adjusted as noted)	\$28,673,724
2014 Rate Case Expense	799,651
2015 RRM Filed Amount	<u>29,473,375</u>
Downward Adjustments:	
Billing Determinant Adjustment	(4,632,888)
AtmoSpirit and Service Awards	(93,977)
Depreciation on Disallowed Projects	(371,598)
Refund from Appeal	(860,257)
Correction from ATM RFI 1-26 and ATM RFI 5-10	(1,525,993)
Correction from ACSC RFI 3-01 and ACSC RFI 3-02	(115,499)
2015 RRM Adjusted	<u>\$21,873,163</u>
Total Increase in Base Rates for 2014 RRM and 2015 RRM	\$65,692,051

An increase of about \$21.87 million over the rates Atmos is *currently* charging related to the 2015 RRM, represents an increase of about 4%, and the impact on an average customer's bill would be as follows:

Customer Class	Current Bill	Proposed Bill	Difference	% Increase with Gas Cost	% Increase without Gas Cost
Residential	\$71.48	\$72.62	\$1.14	1.59%	4.45%
Commercial	\$280.04	\$282.73	\$2.69	0.96%	4.01%
Industrial	\$1,082.55	\$1113.37	\$30.82	2.85%	3.66%
Transportation	\$909.36	\$940.17	\$30.81	3.39%	3.70%

The rate schedules to accomplish the increase are attached to the Resolution approving the increase.

The City should take action as soon as possible but no later than May 31, 2015.

ATTACHMENT A TO AGENDA INFORMATION SHEET

SETTLEMENT AGREEMENT BETWEEN ATMOS ENERGY CORP., MID-TEX DIVISION AND ATMOS TEXAS MUNICIPALITIES

WHEREAS, this agreement ("Settlement Agreement") is entered into by Atmos Energy Corp.'s Mid-Tex Division and Atmos Texas Municipalities ("ATM") whose members include the Cities of Austin, Balch Springs, Bandera, Bartlett, Belton, Blooming Grove, Bryan, Cameron, Cedar Park, Clifton, Corsicana, Denton, Electra, Fredericksburg, Gatesville, Georgetown, Glen Rose, Goldthwaite, Granbury, Greenville, Groesbeck, Hamilton, Heath, Henrietta, Hickory Creek, Hico, Hillsboro, Lampasas, Leander, Lometa, Longview, Marble Falls, Mart, Mexia, Olney, Pflugerville, Point, Princeton, Ranger, Rice, Riesel, Rockdale, Rogers, Round Rock, San Angelo, Sanger, Somerville, Star Harbor, Trinidad, and Whitney.

WHEREAS, on February 28, 2014, Atmos filed with the ATM Cities an application, hereinafter referred to as the 2014 RRM filing, to adjust rates pursuant to Rider RRM - Rate Review Mechanism, which were subsequently consolidated into GUD No. 10359 at the Railroad Commission of Texas; and

WHEREAS, on February 27, 2015, Atmos filed with the ATM Cities an application, hereinafter referred to as the 2015 RRM filing, to adjust rates pursuant to Rider RRM - Rate Review Mechanism; and

WHEREAS, the Settlement Agreement resolves all issues between Atmos and ATM ("the Signatories") regarding the 2014 RRM filing, which is currently pending before the Commission, and the 2015 RRM filing, which is currently pending before the ATM Cities, in a manner that the Signatories believe is consistent with the public interest, and the Signatories represent diverse interests; and

WHEREAS, the Signatories believe that the resolution of the issues raised in the 2014 RRM filing and the 2015 RRM filing can best be accomplished by each ATM City approving this Settlement Agreement and the rates, terms and conditions reflected in the tariffs attached to this Settlement Agreement as Exhibit A;

NOW, THEREFORE, in consideration of the mutual agreements and covenants established herein, the Signatories, through their undersigned representatives, agree to the following Settlement Terms as a means of fully resolving all issues between Atmos and the ATM Cities involving the 2014 RRM filing and 2015 RRM filing:

Settlement Terms

1. Upon the execution of this Settlement Agreement, the ATM Cities will approve an ordinance or resolution to approve the Settlement Agreement and implement the rates, terms and conditions reflected in the tariffs attached to the Settlement Agreement as Exhibit A. (Attachment A to the Resolution ratifying the Agreement). Said tariffs should allow Atmos to recover annually an additional \$65.7 million in revenue over the amount allowed under currently approved rates by implementation of rates shown in the proof of revenues attached as Exhibit B. (Attachment B to the Resolution ratifying this Agreement). The uniform implementation of gas rates, terms and conditions established by the Settlement Agreement shall be effective for bills

rendered on or after June 1, 2015. Consistent with the City's authority under Section 103.001 of the Texas Utilities Code, the Settlement Agreement represents a comprehensive settlement of gas utility rate issues affecting the rates, operations and services offered by Atmos within the municipal limits of the ATM Cities arising from Atmos' 2014 RRM filing and 2015 RRM filing. No refunds of charges billed to customers by Atmos under the RRM in past periods shall be owed or owing.

2. In an effort to streamline the regulatory review process, Atmos and the ATM Cities have agreed to continue discussions regarding renewal of the Rate Review Mechanism ("Rider RRM"). To that end, Atmos and the ATM Cities agree to begin such discussions no later than the date upon which Atmos submits its next application under the existing RRM.
3. Atmos and the ATM Cities agree that rate base as of December 31, 2014 in the amount of \$1,955,948,256 is just and reasonable and shall be recovered in rates.
4. Atmos and the ATM Cities agree that a pension and other postemployment benefits balance as of December 31, 2014 in the amount of \$18,284,949 is just and reasonable and shall be used as the beginning balance for purposes of determining pension and other postemployment benefits to be recovered in the next RRM filing (Attachment C to the Resolution ratifying the Agreement).
5. With regard to the treatment of Atmos' Rule 8.209 regulatory asset under the RRM, Atmos and the ATM Cities agree to the following with respect to any pending and future RRM filings:
 - a. the capital investment in the Rule 8.209 regulatory asset in the 2014 RRM filing and 2015 RRM filing is reasonable and consistent with the requirements of Rule 8.209;
 - b. the classification of projects included in the Rule 8.209 regulatory asset in the 2014 RRM filing and 2015 RRM filing is reasonable and consistent with the requirements of Rule 8.209 and shall serve as a basis for classification of projects in future RRM filings;
 - c. the treatment of blanket replacement projects, system upgrades, relocations, and transmission line replacements in the Rule 8.209 regulatory asset in the 2014 RRM filing and 2015 RRM filing is reasonable and consistent with the requirements of Rule 8.209 and shall be included in future RRM filings.
 - d. the incurred expenses included in the Rule 8.209 regulatory asset in the 2014 RRM and the 2015 RRM are reasonable and consistent with the requirements of Rule 8.209 and shall be included in future RRM filings;
 - e. interest on the Rule 8.209 regulatory asset account shall be calculated using the pre-tax cost of capital most recently approved by the Commission. The use of the pre-tax cost of capital is consistent with Rule 8.209. A return on Rule 8.209 capital investment is only earned once the investment is included in rate base. No

change in the Company's calculation of the interest component in its Rule 8.209 regulatory asset accounts is warranted through the period ended May 31, 2015. Beginning June 1, 2015, interest expense shall be calculated monthly using simple interest (*i.e.* 11.49% divided by 12, or approximately 0.96% per month) applied to the total value of the Rule 8.209 asset investment (exclusive of interest) until such time the Rule 8.209 regulatory asset is approved for inclusion in the Company's rate base.

- f. While Atmos and the ATM Cities agree to apply the treatments and methodologies set forth in this paragraph, subsections (a) – (e) in all future RRM filings, the regulatory authority retains its right to disallow any capital investment that is not shown to be prudently incurred in future RRM filings.
 - g. Atmos and the ATM Cities acknowledge that their agreement regarding the treatment and methodologies applicable to Rule 8.209 capital investments under the RRM tariff shall not prejudice the right of either party to argue for different treatments or methodologies in a future statement of intent proceeding.
- 6. Revenues approved pursuant to Paragraph 1 of the Settlement Agreement include reimbursement of all rate case expenses owed to the ATM Cities in connection with the 2014 RRM filing.
 - 7. The Signatories agree that each ATM city shall approve this Settlement Agreement and adopt an ordinance or resolution to implement for the ATM Cities the rates, terms, and conditions reflected in the tariffs attached to the Settlement Agreement as Exhibit A. Atmos and ATM further agree that at such time as all of the ATM Cities have passed an ordinance or resolution consistent with the Settlement Agreement and Atmos has received such ordinance or resolution, Atmos shall withdraw its appeal of the currently pending RRM filing before the Railroad Commission of Texas in connection with the 2014 RRM filing.
 - 8. Atmos and the ATM Cities further agree that the express terms of the Rider RRM are supplemental to the filing, notice, regulatory review, or appellate procedural process of the ratemaking provisions of Chapter 104 of the Texas Utilities Code. If the statute requires a mandatory action on behalf of the municipal regulatory authority or Atmos, the parties will follow the provisions of such statute. If the statute allows discretion on behalf of the municipal regulatory authority, the ATM Cities agree that they shall exercise such discretion in such a way as to implement the provisions of the RRM tariff. If Atmos appeals an action or inaction of an ATM City regarding an RRM filing to the Railroad Commission, the ATM Cities agree that they will not oppose the implementation of interim rates or advocate the imposition of a bond by Atmos consistent with the RRM tariff. Atmos agrees that it will make no filings on behalf of its Mid-Tex Division under the provisions of Section 104.301 of the Texas Utilities code while the Rider RRM is in place. In the event that a regulatory authority fails to act or enters an adverse decision regarding the proposed annual RRM adjustment, the Railroad Commission of Texas shall have exclusive appellate jurisdiction, pursuant to the provisions of the Texas Utilities Code, to review the action or inaction of the regulatory authority exercising exclusive original jurisdiction over the RRM request.

In addition, the Signatories agree that this Settlement Agreement shall not be construed as a waiver of the ATM Cities' right to initiate a show cause proceeding or the Company's right to file a Statement of Intent under the provisions of the Texas Utilities Code.

9. The Signatories agree that the terms of the Settlement Agreement are interdependent and indivisible, and that if any ATM city enters an order that is inconsistent with this Settlement Agreement, then any Signatory may withdraw without being deemed to have waived any procedural right or to have taken any substantive position on any fact or issue by virtue of that Signatory's entry into the Settlement Agreement or its subsequent withdrawal. If any ATM city rejects this Settlement Agreement, then this Settlement Agreement shall be void *ab initio* as to that city.
10. The Signatories agree that all negotiations, discussions and conferences related to the Settlement Agreement are privileged, inadmissible, and not relevant to prove any issues associated with Atmos' 2014 RRM filing and 2015 RRM filing.
11. The Signatories agree that neither this Settlement Agreement nor any oral or written statements made during the course of settlement negotiations may be used for any purpose other than as necessary to support the entry by the ATM Cities of an ordinance or resolution implementing this Settlement Agreement.
12. The Signatories agree that this Settlement Agreement is binding on each Signatory only for the purpose of settling the issues set forth herein and for no other purposes, and, except to the extent the Settlement Agreement governs a Signatory's rights and obligations for future periods, this Settlement Agreement shall not be binding or precedential upon a Signatory outside this proceeding.
13. The Signatories agree that this Settlement Agreement may be executed in multiple counterparts and may be filed with facsimile signatures.

Agreed to this 7 day of May, 2015.

ATMOS ENERGY CORP., MID-TEX DIVISION

By: John A. Paris
John A. Paris
President, Mid-Tex Division

Agreed to this 7th day of May 2015.

ATTORNEY FOR ATMOS TEXAS MUNICIPALITIES, WHOSE MEMBERS INCLUDE THE CITIES OF AUSTIN, BALCH SPRINGS, BANDERA, BARTLETT, BELTON, BLOOMING GROVE, BRYAN, CAMERON, CEDAR PARK, CLIFTON, CORSICANA, DENTON, ELECTRA, FREDERICKSBURG, GATESVILLE, GEORGETOWN, GLEN ROSE, GOLDTHWAITE, GRANBURY, GREENVILLE, GROESBECK, HAMILTON, HEATH, HENRIETTA, HICKORY CREEK, HICO, HILLSBORO, LAMPASAS, LEANDER, LOMETA, LONGVIEW, MARBLE FALLS, MART, MEXIA, OLNEY, PFLUGERVILLE, POINT, PRINCETON, RANGER, RICE, RIESEL, ROCKDALE, ROGERS, ROUND ROCK, SAN ANGELO, SANGER, SOMERVILLE, STAR HARBOR, TRINIDAD, AND WHITNEY.

By:


Alfred R. Herrera*

* Subject to approval by ATM City Councils