

AGENDA INFORMATION SHEET
AGENDA ITEM NO. _____

**DENIAL OF ATMOS ENERGY CORPORATION, MID-TEX DIVISION'S
(ATMOS) REQUEST TO INCREASE ITS REVENUE AND CHANGE ITS
RATES UNDER THE RATE REVIEW MECHANISM**

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. Both 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

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%

Prior Increase Under the 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.

Less than a year ago, on or around July 15, 2013, Atmos submitted a request to increase rates under the 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%.

RATE REVIEW MECHANISM

On February 28, 2013, Atmos initiated a ratemaking proceeding with cities in the coalition known as the Atmos Texas Municipalities (ATM) by submitting an application to increase its revenue by about \$45.6 million and to change its rates to collect that increase in revenue. An increase of \$45.6 million represents an increase of about 9.2% in annual base-rate revenue. The increase for an average customer is as follows:

Residential Customer:	\$2.02/month (9.96%) in base rates.
Commercial Customer:	\$2.16/month (10.16%) in base rates.
Industrial/Transportation Customer:	\$53.65/month (10.29 %) in base rates.

ATM retained the law firm of Herrera & Boyle, PLLC (H&B) as Special Counsel and the consulting firm of Utilitech, Inc. (Utilitech) to review Atmos' filing. After an extensive review of Atmos' request to increase its revenue and change its rates, on about April 10, 2014, ATM's Special Counsel and consultants concluded Atmos merited an increase of no more than about \$26.6 million. Special Counsel's and the consultants' assessment was preliminary and excluded additional downward adjustments to Atmos' request that are not included in the \$26.6 million amount because of the amount of time to review Atmos' request and because of then-outstanding responses to requests for information submitted to Atmos by ATM's Special Counsel.

The basis for ATM's consultants' preliminary assessment that Atmos warranted at most an increase of \$26.6 million is based on numerous exclusions of costs or rejection of accounting practices for which Atmos failed to carry its burden of proof that such costs or practices were reasonable and consistent with sound ratemaking and regulatory principles. Examples of these items included Atmos' request with regard to:

- An increase in Uncollectible Revenue related to implementation of a new billing system and unexplained cost overruns associated with implementation of the new billing system
- An increase in promotional advertising expenses unrelated to the conservation of energy and more related to promoting Atmos' corporate image
- Atmos' Incentive Compensation program for its executives and upper management
- Inclusion in its capital accounts of items the Railroad Commission had in prior orders excluded from Atmos' cost of service
- Atmos' use of projected costs related to medical and dental benefits
- Atmos' deferred accounting treatment of certain pension benefits
- The amount of Cash Working Capital Atmos proposed to recover from customers
- Atmos' treatment of certain federal income tax expenses including its ratemaking treatment of accumulated deferred income tax (ADIT) reserves
- Atmos' calculation of accounting balances related to certain regulatory assets allowed under the Railroad Commission's rules

This is not intended to be nor is it an exhaustive list of the issues identified by ATM's rate experts. It is provided to show some of the areas in Atmos' application to change rates in which ATM's Special Counsel and rate experts found deficiencies in Atmos' request.

ATM's Special Counsel and consultants engaged in good-faith negotiations with Atmos to attempt to reach a settlement of Atmos' proposed increase, but those negotiations failed to produce an agreement.

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

- Option 1.** To deny Atmos' requested increase and approve no increase;
- Option 2.** To deny Atmos' requested increase and approve an increase of no more than \$26.6 million, based on ATM's consultants' preliminary report; or
- Option 3.** To take no action and allow Atmos' proposed increase of \$45.6 million and its related rates to go into effect.

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 \$45.6 million effective June 1, 2014, 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.

RECOMMENDATION:

ATM's experts' preliminary report suggests Atmos does not warrant an increase of \$45.6 million. Given that the ATM cities and Atmos were not able to reach agreement on an amount by which to increase Atmos' annual revenue and that ATM's Special Counsel and rate experts believe a much lower increase is in order, and in light of the significant increases Atmos has obtained in the recent past, ATM's Special Counsel recommends that the City deny Atmos' proposed increase in revenue and changes in rates.

Atmos will appeal the City's decision denying its requested increase and changes in rates to the Railroad Commission. ATM's Special Counsel recommends that the City participate in Atmos' appeal to the Railroad Commission and in any appeals to the courts of the Railroad Commission's decision.

The attached Resolution also directs Atmos to reimburse ATM's rate-case expenses incurred to date and to reimburse on a monthly basis, ATM's rate-case expenses for any and all related appeals.

The City should take action as soon as possible but no later than May 31, 2014.