

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the matter of United Cities Gas	)	
Company's Purchased Gas Adjustment	)	
Tariff Revisions to be Reviewed in Its	)	Case No. GR-2001-397
2000-2001 Actual Cost Adjustment.	)	

**ATMOS ENERGY CORPORATION'S
RESPONSE TO STAFF RECOMMENDATION**

COMES NOW Atmos Energy Corporation, formerly known as United Cities Gas Company¹ ("Atmos" or "Company"), and pursuant to the Commission's Order Modifying Procedural Schedule issued on March 28, 2002, states its response to the Staff's Recommendation filed on August 29, 2002, as follows:

1. On August 29, 2002, the Commission Staff filed its recommendation following completion of the audit of the 2000-2001 Actual Cost Adjustment ("ACA") filing for what was formerly Atmos' United Cities Gas Company division. The Staff's audit consisted of an analysis of the billed revenues and actual gas costs included in the Company's computation of the ACA for the 2000-2001 period. The Company will respond to the various issues identified by Staff in the following paragraphs.

2. In the "Purchasing Practices" section of the Staff Recommendation, Staff comments upon the Company's hedging and storage practices as follows:

In the review of Company purchasing practices for the Consolidated district, the Staff reviewed the Company's decisions regarding flowing supplies and planned storage withdrawals for the ACA period.

¹ Since October 1, 2002, Atmos Energy Corporation has operated all its various divisions using the name of "Atmos Energy." For purposes of the Missouri currently effective tariff, the former United Cities Gas Company division which is the subject of this proceeding is now referred to as "Area P" (Palmyra area) and "Area U" (remainder of United Cities division).

The Staff believes that it was reasonable to expect United Cities to hedge a minimum level of its natural gas purchases for the winter months of the ACA period. The Staff believes 30% of normal requirements, as a minimum level of hedging for each month during the period of November 2000 through March 2001, is reasonable. Normal requirements are the amount of storage withdrawals and purchases the Company needs to make on a monthly basis in order to meet its demand based upon normal weather. The 30% of normal requirements minimum should not be viewed either as an optimal level or as precedent for future hedging levels, but only as a minimum level that was reasonable and attainable for the winter of 2000/2001. The Staff compared the Company's planned monthly hedged volumes with the monthly 30% of normal requirements. The hedged volumes include storage and fixed price purchases. The Company plan met the 30% threshold for November 2000 through January 2001, but the planned hedged volumes for February and March 2001 were only 14.1% and 23.2% of normal requirements. As a result of this review, Staff proposes a hedging adjustment of (\$105,326) for the Consolidated district to reflect the Company's hedging activity shortfall during the 2000-2001 ACA winter period.

In addition, the Staff reviewed United Cities' use of the hedged volumes from its storage resources during the winter of 2000/2001. Storage is an integral part of this Company's hedging efforts and must be considered when the hedging plan is developed and implemented. The Company's level of storage withdrawals are affected by the planned level of flowing supplies. Flowing supply means gas that is purchased for current consumption and not taken from storage.

Given the information available to the Company when decisions were made regarding planned flowing volumes and storage withdrawals for November 2000 through March 2001, Staff believes that United Cities relied too heavily on flowing supplies in January 2001, given that storage inventory was at 394,236 MMBtu at the end of December 2000. Staff believes that United Cities could have reasonably avoided much of its customers' exposure to the higher flowing gas costs in January 2001 by following a reasonable approach for planned flowing gas and storage withdrawals for that month. The Company offered no explanation for the level of flowing supplies in January 2001. United Cities' plans for flowing gas and storage withdrawals had an unfavorable economic impact on purchased gas costs of \$454,763 and the Staff proposes to reduce gas costs by this amount. The total proposed purchasing practices adjustment is (\$105,326 + \$454,763), or \$560,089).

3. The Company strongly disagrees with the above-quoted Staff's comments and disallowance of \$560,089 related to hedging practices and storage utilization. A disallowance of this magnitude would be financially detrimental to the Company's ability to provide reliable service throughout its Missouri service areas. In addition, the Staff's proposed adjustments appear to be based primarily on the use of hindsight. Few LDCs in Missouri were utilizing hedging techniques and storage utilization to an exact pre-determined level during this period, as now recommended as appropriate by Staff. Gas purchasing and storage utilization plans are utilized as tools to plan storage and supply requirements and are reviewed and adjusted throughout the period based on the level of storage utilized each month and the inventory required for future winter months in order to meet the requirements of a late peak day requirement. It is unreasonable and unlawful to hold the Company after-the-fact to a standard that had not been previously articulated or adopted by the Commission or otherwise considered reasonable by the LDC industry, at the time the Company was making its decisions.

With regard to its "hedging" disallowance, Staff is recommending a reduction in gas costs of \$105,326. Staff reaches its conclusion by applying a 30% hedging standard to normal requirements as if it were a preexisting standard at the time Company made its decisions in 2000-2001. The Company believes that Staff has no basis to apply this 30% standard to the Company, based upon the use of hindsight. At no time before or during the 2000-2001 heating season was the expectation of having a minimum of 30% of normal requirements hedged ever articulated by Staff or the Commission. As recognized by Staff, the Company exceeded a 30% threshold in November 2000 through January 2001. However, it is inappropriate to penalize the Company for not meeting an unarticulated standard of 30% for February and March 2001, as recommended by Staff.

The Staff's proposed disallowance of \$454,763 related to the Company's use of storage is also inappropriate. On the Panhandle Eastern Pipeline (PEP) system that encompasses the Missouri service area of Hannibal, Canton, Palmyra, and Bowling Green, the Company serves over 13,800 customers of which 12,160 are residential customers. Company is contracted for storage service to balance the system usage with first-of-month and incremental daily gas requirements. The Neeleyville system serves approximately 500 customers and is served by Texas Eastern and NGPL pipelines.

Company's load requirements are very heat sensitive due to the residential core customer base and therefore are very difficult to manage on a daily basis. The weather can and does have a significant impact on the amount of gas that may be withdrawn or injected during the course of a month. The contractual nature of the storage services allows Company to preset the nominated daily and/or No-Notice storage service. The withdrawal quantities are determined by the forecasted daily customer's requirements which are subject to daily fluctuations due to actual weather conditions. As the storage level is depleted, Company is required to make adjustments based on remaining levels to maintain peaking capabilities throughout the winter season. Therefore, since the storage services are primarily used for operational balancing, and Company experienced colder than normal November and December periods, which resulted in heavier than anticipated withdrawals from storage, Company made an operational decision to purchase additional flowing gas for the system during January. The weather for the first week of January was forecasted to be at or below normal and the possibility existed that the trend would continue for a colder than normal January and February. Based upon this possibility, Company made an operational decision to purchase additional flowing gas in December to meet January demand in an effort to protect further erosion of existing storage levels. The actual weather for January was

101% of normal, and Company's operational decision to purchase additional flowing gas, allowed it to mitigate the risk of inadequate storage in meeting future peaking conditions on the system in February and March. This resulted in a very small quantity of withdrawals in January. In addition to the storage inventory concern stated above, Company was concerned that the price increases that occurred in late 2000 would not stop at the \$10 per MMBtu price (with a colder than normal January) but would continue to increase for incremental supply that would have been required if flowing supplies were added during the month.

During the 2000-2001 winter, Company had not yet implemented its hedging program utilizing financial hedges. However, it did fix the price for a portion of its purchases using fixed price contracts. Since Neeleyville and the Hannibal, Canton, Palmyra and Bowling Green areas all fall within the same rate district, the Company decided the best approach was to fix the price for the supply of the larger systems (i.e. Hannibal, Canton, Palmyra and Bowling Green) for fixing the price. The reason for this approach was to insure that the quantities fixed could flow each day of the month. Staff's proposed adjustment totally overlooks these practical and operational concerns.

For these reasons, the Staff should reconsider its \$560,089 disallowance related to the Company's purchasing practices.

4. The Commission Staff also recommends that the Company submit a copy of the Company's policies and procedures for those responsible for nominating natural gas by December 1, 2002. The Company would note that the Commission Staff recently concluded a management audit that included a review of the Company's policies and procedures for nominating natural gas. The Commission Staff did not make any recommendations for improvement in its nomination processes. The Company therefore believes it would be

duplicative to re-submit these policies for a second review by the Commission Staff within a few months of the completion of the management audit.

5. The Company will accept Staff's other proposed adjustments discussed in the "Deferred Carrying Cost Balances" and "Propane" sections of the Staff Recommendation. In addition, the Company will accept Staff's recommendation that additional documentation regarding the reliability information be submitted by February 3, 2003.

WHEREFORE, Atmos Energy Corporation respectfully requests the Staff reconsider its position on the gas purchasing practices of the Company, and further requests that the Commission issue its order consistent with the Company's response herein.

Respectfully submitted,

/s/ James M. Fischer

James M. Fischer MBN 27543

Larry W. DORITY MBN 25617

FISCHER & DORITY, P.C.

101 Madison, Suite 400

Jefferson City, Missouri 65101

Telephone: (573) 636-6758

Facsimile: (573) 636-0383

E-mail: jfischerpc@aol.com

lwORITY@sprintmail.com

Attorneys for Atmos Energy Corporation, formerly
known as United Cities Gas Company

CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of this document has been hand-delivered, emailed or mailed, First Class, postage prepaid, this 25th day of October, 2002, to:

Dana K. Joyce, General Counsel
Missouri Public Service Commission
P.O. Box 360
Jefferson City, MO 65102

Office of the Public Counsel
P.O. Box 7800
Jefferson City, MO 65102

/s/ James M. Fischer

James M. Fischer