

MODEL STAFF REPORT

The City, along with 150 other cities served by Atmos Energy Mid-Tex Division ("Atmos" or "Company"), is a member of the Atmos Cities Steering Committee ("ACSC"). On April 14, 2008, Atmos filed with the City an application to increase natural gas rates pursuant to the Rate Review Mechanism ("RRM") tariff approved by the City earlier this year. The Company's April RRM filing seeks a \$33.5 million rate increase. The City worked with ACSC to analyze the schedules and evidence offered by Atmos to support its request to increase rates. The Ordinance and attached tariff approving rates that will increase the Company's revenues by \$20 million effective October 1, 2008, are the result of negotiation between ACSC and the Company to resolve issues raised by ACSC during the review and evaluation of ACSC's RRM filing. The monthly bill impact for the average residential customer is \$0.81. The ACSC Executive Committee recommends that all ACSC cities adopt the ordinance implementing the rate change.

RRM Background:

The RRM tariff was approved by cities as part of the settlement agreement to resolve Atmos' 2007 rate increase case. Atmos' rate request represents the first filing pursuant to the three-year trial project known as the RRM process. The RRM process was created collaboratively by the Steering Committee and Atmos as an alternative to the GRIP surcharge process. The RRM process allows for a more comprehensive rate review and annual adjustment that will function as a substitute for future GRIP filings during the three-year trial period specified by the tariff.

There are two components to the RRM adjustment. The prospective component adjusts rates for known and measurable changes in O&M and net plant investment. Atmos and ACSC agreed to cap changes to expenses and invested capital at no more than five percent. The true up component evaluates whether the Company has over or underrecovered its earnings for the previous year. For purposes of the RRM true up component, Atmos' rate of return on equity and its capital structure are frozen to avoid the parent company from manipulating the overall rate of return. Costs expressly prohibited from recovery through the RRM include first class air-fare, travel, meals or entertainment for employee's spouse, alcohol, sports events, entertainment, arts and cultural events, sponsorship of sports, arts or cultural events, and social club membership dues.

Purpose of the Ordinance:

The purpose of the Ordinance is to approve rate tariffs (Attachment A) that reflect the negotiated rate change pursuant to the RRM process. The Ordinance also approves the Company's proof of revenues (Attachment B), a required part of the RRM filing.

As a result of the negotiations, ACSC was able to reduce the Company's requested \$33.5 million RRM increase by more than 35 percent. Approval of the Ordinance will result in rates that implement a \$20 million increase in Atmos' revenues effective October 1, 2008.

Reasons Justifying Approval of the Negotiated Resolution:

During the time that the City has retained original jurisdiction in this case, consultants working on behalf of ACSC cities have investigated the support for the Company's requested rate increase. While the evidence does not support the \$33.5 million increase requested by the Company, ACSC consultants agree that the Company can justify an increase in revenues of at least \$19.8 million.

A contested case proceeding before the RRC on the Company's current application will take several months and cost ratepayers millions of dollars in rate case expenses and would not likely produce a request more favorable than that to be produced by the settlement. The ACSC Executive Committee recommends that ACSC members take action to approve the ordinance authorizing new rate tariffs.

Explanation of "Be It Ordained" Paragraphs:

1. This paragraph approves all findings in the ordinance.
2. This section adopts the attached tariffs (Attachment A) and Company's proof of revenues (Attachment B) in all respects and finds the rates set pursuant to the attached tariffs to be just, reasonable and in the public interest. Note that only new tariffs or existing tariffs that are being revised are attached to the Ordinance. Existing tariffs that are not being changed in any way are not attached to the Ordinance.
3. This section repeals any resolution or ordinance that is inconsistent with this Ordinance.
4. This section finds that the meeting was conducted in compliance with the Texas Open Meetings Act, Texas Government Code, Chapter 551.
5. This section is a savings clause, which provides that if any section(s) is later found to be unconstitutional or invalid, that finding shall not affect, impair or invalidate the remaining provisions of this Ordinance. This section further directs that the remaining provisions of the Ordinance are to be interpreted as if the offending section or clause never existed.
6. This section is a "Most Favored Nations" clause, which protects the City by mandating that if a Final Order or subsequent agreement approved in any proceeding addressing the issues raised in Atmos' RRM filing results in rates or terms that would be more beneficial to the ACSC Cities than the terms of this tariff, the City may, at its option, implement such more favorable rates or terms. The exercise of this right is contingent upon the City agreeing to adopt the terms of the Final Order or subsequent agreement *in toto*.
7. This section provides for an effective date upon passage.
8. This paragraph directs that a copy of the signed resolution be sent to a representative of the Company and legal counsel for ACSC.