




## MEMORANDUM

TO: Mayor and City Council

FROM: Leslie Browder, Chief Financial Officer   
Rondella M. Hawkins, Manager of Telecommunications & Regulatory Affairs

DATE: June 16, 2009

SUBJECT: Update on Texas Gas Service Rates

The purpose of this memorandum is to update you on the results of our review of the documentation associated with a request from Texas Gas Service (TGS) to increase the rates charged to central Texas service area customers. The City Council is scheduled to consider this request on June 18, 2009, as part of a public hearing to be held that evening. Summary information regarding the public hearing and the TGS request can be found as part of Request for Council Action No. 74 on the agenda for June 18, 2009. As a point of reference, rates were last increased in 1993, when Southern Union Gas Company was the natural gas provider in the central Texas area.

### **BASE INCREASE IN REVENUE OF \$1.05 MILLION**

TGS initially requested an increase in base rates that was expected to generate an additional \$3.5 million in annual revenue. The City retained the services of Fox, Smolen and Associates (FSA) to help analyze the underlying documentation to support TGS' request. The City also retained Mr. Alfred Herrera of the law firm Herrera & Boyle to provide legal advice concerning the rate request. Based on FSA's analysis and review of TGS' records and discussions with their financial and ratemaking staff, FSA and Mr. Herrera have concluded that an increase of about \$1.05 million can be supported and would likely be found reasonable by the Railroad Commission of Texas based on their published ratemaking guidance.

As part of this settlement process, the City will have to enter a limited number of specific findings regarding TGS' cost of service related to depreciation rates, return on equity, and capital structure. FSA and outside counsel have indicated to TGS that a return on equity of 10.5% and a capital structure of 49% in long-term debt and 51% in equity is reasonable for purposes of ratemaking under this settlement. TGS concurs with these findings. FSA has noted that the most recent return on equity approved for a TGS company (in North Texas) was 10.85%. In its original application, TGS also requested approval of an acquisition adjustment to recognize ONEOK's acquisition of the Southern

Union Gas Company, whose assets are part of TGS. As part of this recommended settlement, TGS has agreed to withdraw its request for approval of an acquisition adjustment.

### RECOMMENDED RATE DESIGN

In its original application, TGS requested to increase the fixed customer charge as outlined in the table below. FSA has proposed to limit increases in the customer charge to only \$2.00 for residential and \$1.00 for commercial customers. As part of the settlement, TGS has also agreed to the rate design and customer charges proposed by FSA. The following chart shows the current monthly rates, the original rates requested by TGS, and the rates proposed for adoption under this settlement.

Customer Class	TGS			Settlement
	Monthly	Current	Requested	
Residential	Customer Charge	\$7.75	\$11.25	\$9.75
	Volumetric (All Ccf)	\$0.1579	\$0.0579	\$0.0826
Commercial	Customer Charge	\$11.75	\$15.75	\$12.75
	Volumetric Sales	\$0.1595	\$0.1361	\$0.1301

FSA and Mr. Herrera recommend accepting the customer-class revenue allocation as proposed by TGS. The effect of this allocation methodology helps move each customer class closer to recovering what it costs to provide each class with gas utility service and this can best be accomplished when the proposed change in overall rates is not significant, as is the case here. The estimated monthly impact on the average residential and customer bill is shown in the table below.

	Usage	Current	TGS Recommended	Dollar	Percent	Settlement	Dollar	Percent
	(Ccf)	Rates	Rates	Change	Change	Rates	Change	Change

### RESIDENTIAL

#### Austin

Average bill	31	\$ 43.88	\$ 45.31	\$ 1.43	3.3%	\$ 44.63	\$ 0.75	1.7%
Avg. January bill	72	\$ 0.71	\$ 88.37	\$ (2.34)	-2.6%	\$ 88.64	\$ (2.07)	-2.3%

### COMMERCIAL

#### Austin

Average bill	133	\$164.50	\$ 168.08	\$ 3.58	2.2%	\$ 165.78	\$ 1.28	0.8%
Avg. January bill	209	\$251.05	\$ 253.72	\$ 2.67	1.1%	\$ 250.00	\$ (1.05)	-0.4%

### COST OF SERVICE ADJUSTMENT TARIFF

TGS originally requested approval of a cost-of-service-adjustment (COSA) tariff that would have required TGS to seek a change in rates annually. TGS has agreed to withdraw its request for a COSA tariff.

### **RETURN ON STORED GAS**

TGS and the City have agreed that it is reasonable to allow TGS to recover the cost of its investment in stored gas inventories through a gas cost adjustment and earn a return thereon at its authorized rate of return on the monthly average balance in inventories through the annual reconciliation process. This is consistent with Railroad Commission practices. The proposed tariff language was approved by the Railroad Commission in Gas Utilities Docket 9791.

### **GREEN SAVER PROGRAM**

TGS agrees to implement a Green Saver tariff with some minor changes from the program initially discussed (for example, excluding a 5-year eligibility clause that would have limited eligibility to customers who already had an energy audit performed within the past 5 years), and the parties agree to continue in good faith to discuss possible changes to the proposed tariff that would improve the program, with an eye toward reaching agreement and filing an amended tariff within 120 days following the date the Austin City Council adopts its final ratemaking ordinance in this case.

### **FIXED GAS COST PILOT PROGRAM**

TGS would like the ability to offer a voluntary, fixed gas cost pilot program, which is designed to provide monthly natural gas bills that are predictable and guaranteed, for a fee to ratepayers. The parties agree to continue in good faith to discuss possible changes to TGS' gas cost adjustment tariff that would address the details of the pilot program, with an eye toward reaching agreement and filing an amended tariff within 120 days following the date the Austin City Council adopts its final ratemaking ordinance in this case.

### **SUMMARY**

A base rate increase that generates additional revenue of \$1.05 million is reasonable, particularly when approved in conjunction with the withdrawal of both a COSA tariff proposal, as well as TGS' initial request for an acquisition adjustment related to ONEOK's purchase of Southern Union Gas. FSA has completed a thorough review of the underlying ratemaking documentation submitted by TGS, and our legal team has reviewed and recommends the proposed settlement as well. Please feel free to contact Rondella or me if you have any questions.

xc: Marc A. Ott, City Manager  
Clark Cornwell, Law Department