



MEMORANDUM

TO: Council Public Utilities Committee

FROM: Rondella Hawkins, Telecommunications and Regulatory Affairs (TARA) Officer

DATE: May 19, 2015

SUBJECT: Responses to Questions re: Texas Gas Service

This memorandum is provided as a follow-up to questions asked during the April 15 Public Utilities Committee meeting. The questions and discussion focused on Texas Gas Service's proposed rate increase (Item 6).

Below you will find the specific questions and corresponding responses that were developed by Texas Gas Service and the TARA office.

Please let me know if you have any questions. Thank you.

cc:

Robert Goode, Assistant City Manager

Mark Washington, Interim Assistant City Manager

Question:

The Company finances plant investments through cash, debt issuance, or stock issuance. Once the plant is in service, the Company may request recovery of its investment in rates. Please explain the financial impact of the lag between when the Company makes investments and when it begins to recover those investments through rates. Please discuss the federal and state mandates that require utilities to replace and upgrade infrastructure and explain the impact to the utility and the customer of these mandates.

Response:

The U.S. Department of Transportation Pipeline and Hazardous Materials Safety Administration (PHMSA) amended the Federal Pipeline Safety Regulations on December 4, 2009, to require operators of gas distribution pipelines to develop and implement a Distribution Integrity Management Program (DIMP) and to create a plan for meeting the program guidelines in 49 CFR Part 192, Subpart P – Gas Distribution Pipeline Integrity Management (IM). The Railroad Commission of Texas also adopted rules requiring distribution pipelines to develop a DIMP plan which are consistent with the federal regulations (See, Rule §8.209). The purpose of the DIMP Plan is to ensure ONE Gas Distribution Companies enhance safety by identifying and reducing gas distribution integrity risks.

The Company's DIMP Plan establishes a process to identify existing and potential threats to the gas distribution pipeline such as corrosion, natural forces, excavation damage, material or welds, equipment failure and other concerns that could threaten the integrity of the pipeline. Risk assessment is an ongoing process of understanding what factors affect the risk posed by threats to the gas distribution pipeline system and where a particular risk ranks relative to others. The primary objectives of the evaluation and ranking of a gas distribution pipeline system risk are to:

- Consider each applicable current and potential threat;
- Determine the applicability of each threat;
- Consider the likelihood of occurrence associated with each threat;
- Consider the potential consequences of an occurrence;
- Rank the risks (i.e. determine the relative ranking) posed to the pipeline; and
- Consider the relevance of threats in one (1) location to other areas.

The Company continually assesses the state of our systems; ranks system needs according to risk; and then, makes repairs as necessary to provide safe and reliable service. Often, replacement of pipeline is the identified remedy.

Managing leaks is an important part of addressing the integrity of the system. The Railroad Commission of Texas has rules in place governing leak survey in its Rule §8.206(b). TGS complies with this Rule by electing a prescriptive program for leak survey. Under the prescriptive program, the Railroad Commission of Texas requires that TGS conduct leak surveys no less frequently than:

- (1) annually for all systems within a business district;
- (2) every five years for non-business district polyethylene systems or segments within a system;
- (3) every three years for all other non-business district cathodically protected steel systems or segments within a system; and
- (4) every two years for all other non-business district systems or segments within a system

Compliance with these federal and state rules and regulations is mandatory; however, the practices adopted by TGS are also those of a responsible company striving to provide safe and reliable natural gas service. The Company believes safety is our utmost priority and we take our responsibilities seriously. We continually update our records and data and identify what appropriate projects need to be completed to replace aging infrastructure over a reasonable period of time. The capital costs associated with these types of regulatory compliance are included in the Company's GRIP filings. Additionally, capital costs associated with new installations, government relocations/replacements, computer hardware, software, and other office equipment necessary for operating a natural gas utility are included in the GRIP filings.

While the Company incurs costs for capital investments at the time materials are purchased and installed, it cannot request recovery of these costs unless the investments are in-service during the test year under consideration in a rate filing. Thus, TGS may not begin to recover some of its investments in its rates for service until more than a year after it has expended resources. The impact on the Company can be seen in the Earnings Report that accompanies the GRIP filing each year. Schedule A of the Earnings Report is attached below. In the last rate case it was determined that the Company should have the opportunity to earn a return on its investment of 8.40%. However, the delay or lag between when capital is expended and when recovery is allowed resulted in the Company actually earning a return of 6.60% for 2014. The ability of the Company to earn a return is an important factor in its ability to attract new capital to fund its operations in the most efficient and cost effective manner. Over the last five years, the Company's actual return on rate base has ranged from 5.46% to 7.84% due to this lag.

Schedule A

TEXAS GAS SERVICE COMPANY
CENTRAL TEXAS SERVICE AREA
INTERIM COST RECOVERY AND RATE ADJUSTMENT
TWELVE MONTHS ENDED DECEMBER 31, 2014
EARNINGS REPORT

LINE NO.	DESCRIPTION	TWELVE MONTHS ENDED 12/31/2014
1	Total Operating Revenues	\$137,601,468
2	Operating Expenses:	
3	Gas Costs	(75,873,106)
4	Depreciation & Amortization Expense	(7,580,263)
5	Taxes Other Than Income Taxes	(2,595,117)
6	Miscellaneous Interest Expense	0
7	Interest on Customer Deposits	(7,963)
8	Transmission Expense	(159,880)
9	Distribution Expense	(10,439,418)
10	Customer Accounts Expense	(5,669,628)
11	Administrative and General Expense	(15,683,167)
12	Total Operating Expenses Before Federal Income Taxes	(118,008,543)
13	Total Operating Income Before Federal Income Taxes	\$19,592,925
14	Federal Income Taxes	(5,916,519)
15	Return on Rate Base	\$13,676,406
16	Rate Base	\$207,096,305
17	Percent Return on Rate Base	6.60%
18	Allowed Rate of Return	8.400%

Question:

From the Company's last rate case through this GRIP filing, please provide the following by year:

- a. Date of Filing
- b. Customer Count
- c. Increase in Net Investment
- d. Revenue Increase
- e. Rate by Customer Class
- f. Rate Increase by Customer Class

Response:

Since the rate case filed in 2009, TGS has increased its net investment in the CTX Service Area by over \$127 million. During that same time period, the Company has been granted revenue increases of just over \$20 million. The Company's GRIP filings have been made to recover only increases in capital related expenditures. As mentioned above, these expenditures have been made to meet regulatory mandates, as well as for new installations, government relocations/replacements, computer hardware, software, and other office equipment necessary for operating a natural gas utility. The CTX Service has experienced customer growth during this time with the incorporated customer count increasing by 9.5% since the 2009 rate case. Table 1 below summarizes the customer count, increase in net investment and increase in revenue from the 2009 Rate Case through the current GRIP filing.

Table 1

	2009 Rate Case	2011 GRIP	2012 GRIP	2013 GRIP	2014 GRIP	2015 GRIP
Filing Date	2/11/2009	2/10/2011	2/10/2012	2/11/2013	2/11/2014	2/11/2015
Customer Count (Incorporated)	198,209	205,684	207,959	211,016	214,182	216,982
Increase in Net Investment		\$9,466,027	\$23,922,153	\$29,533,777	\$38,947,812	\$25,139,227
Revenue Increase	\$1,050,000	\$1,540,300	\$3,775,205	\$4,418,980	\$5,664,928	\$3,696,732

Below, Chart 1 demonstrates the increase in Net Investment along with the revenue increase granted in each time period.

Chart 1 – Net Investment and Revenue Increase by Year

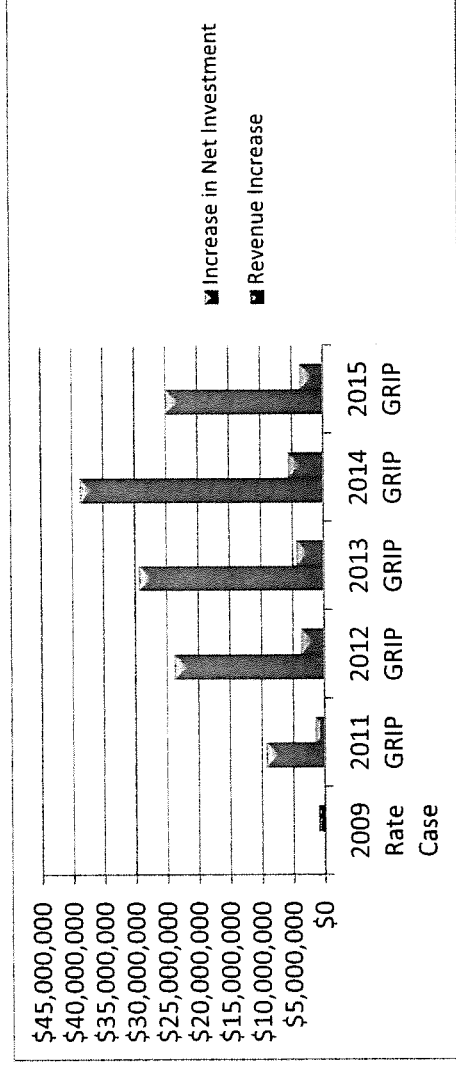


Chart 2, below, demonstrates the incorporated customer count in each year from the rate case filed in 2009 through the current filing.

Chart 2 – Customer Count by Year

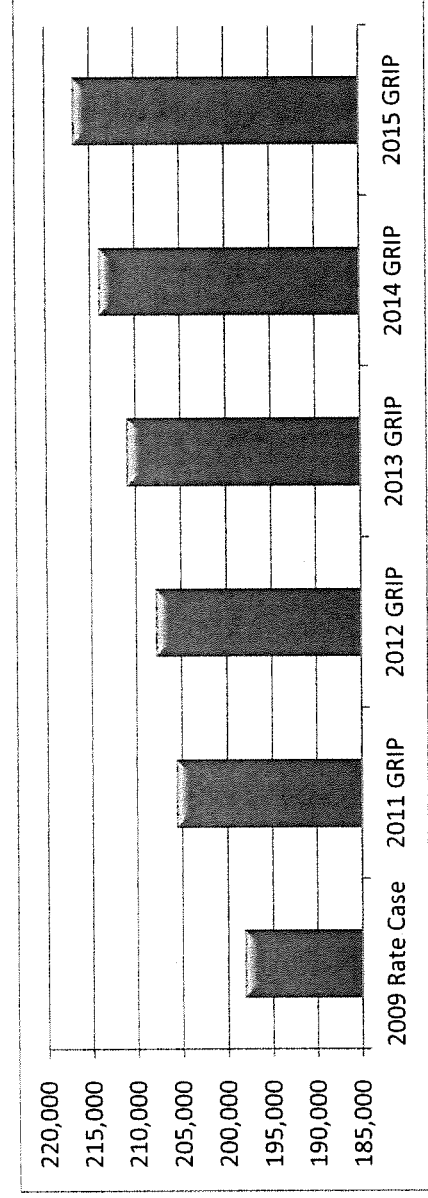


Table 2 provides the customer charge and volumetric rate from the 2009 rate case through the present filing.

Table 2 – Rates by Customer Class

Customer Class	2009 Rate Case		2011 GRIP		2012 GRIP		2013 GRIP		2014 GRIP		2015 GRIP	
	Customer Charge	Volumetric Charge	Customer Charge	Volumetric Charge	Customer Charge	Volumetric Charge	Customer Charge	Volumetric Charge	Customer Charge	Volumetric Charge	Customer Charge	Volumetric Charge
Residential	\$9.75	\$0.08257	\$10.21	\$0.08257	\$11.33	\$0.08257	\$12.62	\$0.08257	\$14.24	\$0.08257	\$15.28	\$0.08257
Commercial	\$12.75	\$0.13010	\$14.36	\$0.13010	\$18.41	\$0.13010	\$23.23	\$0.13010	\$29.42	\$0.13010	\$33.40	\$0.13010
Large Volume Commercial	\$80.00	\$0.10898	\$97.84	\$0.10898	\$158.68	\$0.10898	\$213.67	\$0.10898	\$285.96	\$0.10898	\$331.83	\$0.10898
Industrial	\$40.00	\$0.10675	\$46.26	\$0.10675	\$64.34	\$0.10675	\$88.83	\$0.10675	\$118.27	\$0.10675	\$138.59	\$0.10675
Large Volume Industrial	\$80.00	\$0.10064	\$105.10	\$0.10064	\$166.62	\$0.10064	\$233.09	\$0.10064	\$340.29	\$0.10064	\$430.65	\$0.10064
Public Authority	\$20.00	\$0.11838	\$22.22	\$0.11838	\$27.93	\$0.11838	\$34.14	\$0.11838	\$42.28	\$0.11838	\$47.61	\$0.11838
Large Volume Public Authority	\$80.00	\$0.11041	\$111.13	\$0.11041	\$186.08	\$0.11041	\$267.18	\$0.11041	\$367.35	\$0.11041	\$430.42	\$0.11041
Public School Space Heating	\$40.00	\$0.11689	\$46.86	\$0.11689	\$64.17	\$0.11689	\$79.58	\$0.11689	\$98.51	\$0.11689	\$110.37	\$0.11689
CNG	\$25.00	\$0.07018	\$29.27	\$0.07018	\$38.94	\$0.07018	\$45.07	\$0.07018	\$52.61	\$0.07018	\$57.74	\$0.07018
Commercial Transportation	\$75.00	\$0.13010	\$86.38	\$0.13010	\$113.42	\$0.13010	\$143.01	\$0.13010	\$182.21	\$0.13010	\$206.71	\$0.13010
Large Volume Commercial												
Transportation	\$150.00	\$0.10898	\$187.03	\$0.10898	\$278.54	\$0.10898	\$381.10	\$0.10898	\$523.31	\$0.10898	\$613.52	\$0.10898
Industrial Transportation	\$80.00	\$0.10675	\$97.61	\$0.10675	\$140.33	\$0.10675	\$190.01	\$0.10675	\$257.49	\$0.10675	\$302.96	\$0.10675
Large Volume Industrial												
Transportation	\$150.00	\$0.10064	\$224.19	\$0.10064	\$406.02	\$0.10064	\$512.44	\$0.10064	\$785.28	\$0.10064	\$963.33	\$0.10064
Public Authority Transportation	\$25.00	\$0.11838	\$28.16	\$0.11838	\$34.64	\$0.11838	\$40.80	\$0.11838	\$48.94	\$0.11838	\$53.98	\$0.11838
Large Volume Public Authority												
Transportation	\$100.00	\$0.11041	\$141.64	\$0.11041	\$249.69	\$0.11041	\$352.77	\$0.11041	\$464.62	\$0.11041	\$535.35	\$0.11041
Public School Space Heating												
Transportation	\$60.00	\$0.11689	\$67.03	\$0.11689	\$84.44	\$0.11689	\$104.91	\$0.11689	\$131.29	\$0.11689	\$148.43	\$0.11689
CNG Transportation	\$40.00	\$0.07018	\$41.57	\$0.07018	\$45.42	\$0.07018	\$49.92	\$0.07018	\$55.69	\$0.07018	\$58.70	\$0.07018

Table 3 provides the increase in the customer charge, by customer class, for each year following the 2009 Rate Case through the present filing and the total increase over those five years.

Table 3 – Customer Charge Increase

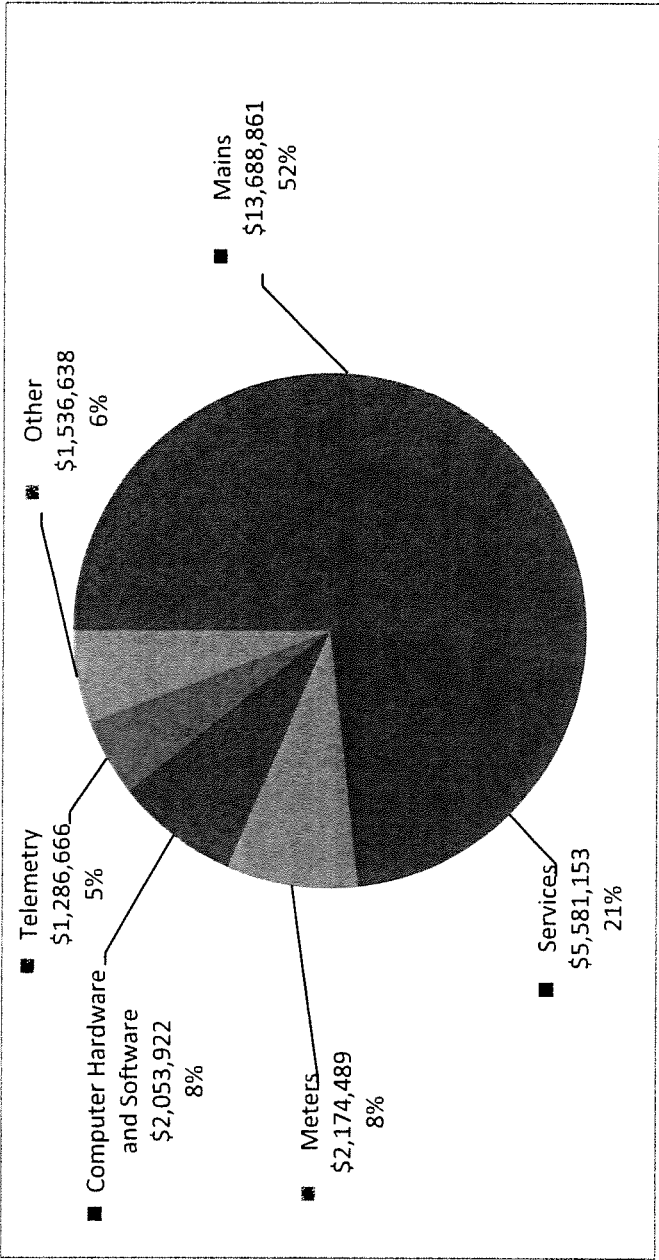
Customer Class	Increase in Monthly Customer Charge (Volumetric Rate Unchanged)					Total Increase Since 2009 Rate Case
	2011 GRIP	2012 GRIP	2013 GRIP	2014 GRIP	2015 GRIP	
Residential	\$0.46	\$1.12	\$1.29	\$1.62	\$1.04	\$5.53
Commercial	\$1.61	\$4.05	\$4.82	\$6.19	\$3.98	\$20.65
Large Volume Commercial	\$17.84	\$60.84	\$54.99	\$72.29	\$45.87	\$251.83
Industrial	\$6.26	\$18.08	\$24.49	\$29.44	\$20.32	\$98.58
Large Volume Industrial	\$25.10	\$61.52	\$66.47	\$107.20	\$90.36	\$350.63
Public Authority	\$2.22	\$5.71	\$6.21	\$8.14	\$5.33	\$27.62
Large Volume Public Authority	\$31.13	\$74.95	\$81.10	\$100.17	\$63.07	\$350.42
Public School Space Heating	\$6.86	\$17.31	\$15.41	\$18.93	\$11.86	\$70.38
CNG	\$4.27	\$9.67	\$6.13	\$7.54	\$5.13	\$32.74
Commercial Transportation	\$11.38	\$27.04	\$29.59	\$39.20	\$24.50	\$131.72
Large Volume Commercial Transportation	\$37.03	\$91.51	\$102.56	\$142.21	\$90.21	\$463.52
Industrial Transportation	\$17.61	\$42.72	\$49.68	\$67.48	\$45.47	\$222.97
Large Volume Industrial Transportation	\$74.19	\$181.83	\$106.42	\$272.84	\$178.05	\$813.32
Public Authority Transportation	\$3.16	\$6.48	\$6.16	\$8.14	\$5.04	\$28.98
Large Volume Public Authority Transportation	\$41.64	\$108.05	\$103.08	\$111.85	\$70.73	\$435.35
Public School Space Heating Transportation	\$7.03	\$17.41	\$20.47	\$26.38	\$17.14	\$88.43
CNG Transportation	\$1.57	\$3.85	\$4.50	\$5.77	\$3.01	\$18.70

Question:

Please provide an explanation of the factors driving the need for the increase.

Response:

2013 to 2014 Change in Gross investment



(continued)

Much of the investment in mains and services in this GRIP filing is driven by regulatory requirements for replacement of pipeline. As mentioned above, the U.S. Department of Transportation Pipeline and Hazardous Materials Safety Administration (PHMSA) amended the Federal Pipeline Safety Regulations on December 4, 2009, to require operators of gas distribution pipelines to develop and implement a Distribution Integrity Management Program (DIMP) and to create a plan for meeting the program guidelines in 49 CFR Part 192, Subpart P – Gas Distribution Pipeline Integrity Management (IM). The Railroad Commission of Texas also has adopted rules requiring distribution pipelines to develop a DIMP plan which are consistent with the federal regulations (*See*, Rule §8.209). The purpose of the DIMP Plan is to ensure ONE Gas Distribution Companies enhance safety by identifying and reducing gas distribution integrity risks.

Approximately 77% of the change in gross investment is safety and reliability related. Safety and reliability related plant includes the replacement of mains, services, measuring and regulating station equipment, meter settings, gate valves, control equipment, replacement of cathodic protection equipment, equipment used to monitor gas quality, monitoring and communicating pressures and volumes; replacement of transmission lines and related equipment; tools, equipment, and vehicles used in maintaining the distribution system; Geographic Information System investments; and, hardware and software used to monitor and manage maintenance of the distribution system. New Installations and government relocations (mostly relocations required by the City of Austin) also contributed to the increase.