REPORT TO THE

GEORGIA PUBLIC SERVICE COMMISSION

ATLANTA GAS LIGHT COMPANY

2024 AFFILIATE AUDIT REPORT

DOCKET NO. 43820

PUBLIC REDACTED

ON BEHALF OF

THE GEORGIA PUBLIC SERVICE COMMISSION STAFF

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ATLANTA GAS LIGHT COMPANY
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DOCKET NO. 42315

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I. EXECUTIVE SUMMARY

A. Scope of Review

J. Kennedy and Associates, Inc. ("Kennedy and Associates"), on behalf of the Georgia Public Service Commission's ("Commission") Public Interest Advocacy Staff ("PIA Staff"), conducted a review of the affiliate costs incurred by Atlanta Gas Light Company ("AGL" or "Company") through charges from Southern Company Services, Inc. ("SCS") and AGL Services Company ("ASC") for the time period January 2019 through December 2023. SCS and ASC are centralized service companies that provide common and shared services to Southern Company first tier affiliates, including Southern Company Gas, and to Southern Company Gas first tier affiliates, including AGL. Southern Company Gas is the holding company that was formerly AGL Resources, Inc. ("AGLR").

This review was conducted to provide current information concerning AGL affiliate transactions for use by the Commission in its ongoing regulatory reviews of AGL expansion, construction, service, and costs recoverable for ratemaking, as well as for other regulatory purposes. This review was not performed for the purpose of assessing SCS's, ASC's, or AGL's compliance with generally accepted accounting principles ("GAAP") or the requirements of the Federal Energy Regulatory Commission ('FERC") or any other regulatory agency. The Commission long has recognized that the financial reporting requirements of GAAP and the

FERC do not control regulatory policy or the types and levels of costs that the Commission allows recovery through the ratemaking process.

To conduct the current review, Kennedy and Associates engaged in a structured process of fact-finding and analyses, which culminated in the development of this 2024 Affiliate Audit Report ("Audit Report"). The fact finding included several sets of written discovery, documents obtained from public sources and from AGL in this and other Commission proceedings, and the analyses summarized in this Audit Report. Finally, we also reviewed the NARUC Guidelines for Cost Allocations and Affiliate Transactions, prior Commission Orders involving AGL, FERC Form 60 reporting for SCS, the 2024 Integrated Capacity and Delivery Plan ("i-CDP"), and prior Georgia Rate Adjustment Mechanism ("GRAM") and quarterly affiliate transaction report filings by AGL.

AGL will be provided the opportunity to comment upon the Findings and Recommendations of this Audit Report during the pendency of this proceeding. Due to time limitations, AGL has not had an opportunity to review this report prior to its issuance. Kennedy and Associates reserves the right to address the Company's comments regarding this report during the pendency of this proceeding.

B. Summary of Findings

Kennedy and Associates has reached numerous findings as the result of the 2024 Affiliate Audit. A more detailed discussion of those findings can be found in the subsequent sections of this Audit Report. Kennedy and Associates has not attempted to quantify adjustments for

regulatory purposes since test year cost amounts will not be known until after AGL makes its 2025 GRAM filing.

- Since the Southern Company acquisition of AGLR on July 1, 2016, centralized services are provided to the Southern Company Gas affiliates, including AGL, by both SCS and ASC, although only ASC charges AGL for the combined SCS charges and ASC charges.

- Centralized service expenses incurred by AGL through charges from ASC, including SCS charges to ASC, have increased substantially following the merger. Total service company expenses charged to AGL were $62.521 million in 2015, the year before the merger. They increased to $65.006 million in 2016, to $69.445 million in 2017, and to $80.130 million in 2018. They further increased to $85.499 million in 2019, to $90.601 million in 2020, to $98.745 million in 2021, to $120.218 million in 2022, and to $132.343 million in 2023. The 2023 amount of $132.343 million results in an increase of 111.7% over the $62.521 million amount in 2015 over a period of eight years.

- ASC charges have increased during the audit period following the divestitures of Southern Company affiliate Gulf Power Company in January 2019, Southern Company Gas affiliates Elizabethtown Gas Company, Elkton Gas Services, Florida City Gas, Nicor Home Services, and Nicor Services during 2018, and Southern Company Gas affiliate Sequent Energy Management, LP during 2021. A reduction in the number and size of affiliates with which to spread costs has resulted in higher costs for the affiliates that remain, all else equal.

- Non-capital expense charges from SCS to its electric affiliates have actually decreased year-to-year during the audit period, while non-capital expense charges from SCS to all its affiliates have been increasing at alarming rates. The SCS expense charges to its affiliates were $838.293 million in 2019 and have grown to $1,002.595 million in 2022. While the 2023 FERC Form 60 was not yet available during the drafting of the Audit Report, 2023 SCS expense charges are expected to increase further. Expense costs originating at SCS and eventually charged to AGL were $30.911 million in 2019, $32.036 million in 2020, $32.540 million in 2021, grew significantly to $41.983 million in 2022, or 29%, and then grew even further to $44.461 million in 2023, or another 6%.

- There have been substantial increases in the number of service company full-time equivalent employees ("FTEs") since the beginning of the audit period and they continue to grow, representing another important factor in the significant increases in affiliate charges to AGL. There were 1,014 FTEs at ASC at the beginning of 2019. That number grew to 1,150 as of the end of 2023 and to 1,174 as of February 21, 2024. That

represents a growth of 159 FTEs from January 1, 2019 until February 21, 2024, an increase of 15.7%. There were 3,760 FTEs at SCS at the beginning of 2019. That number grew to 4,205 as of the end of 2023 and to 4,224 as of February 21, 2024. That represents a growth of 464 FTEs from January 1, 2019 until February 21, 2024, an increase of 12.3%.

- Plant asset costs are incurred for projects initiated by SCS and ASC and are either direct assigned to AGL and one or more other affiliates, or allocated to all of the Southern Company Gas affiliates, including AGL, as part of the ratemaking process. These plant asset costs are mostly technology based but also include other classes of general plant, such as facilities, furniture, and fixtures. Assets are direct assigned, or pushed down, to specific ASC affiliates when they benefit those specific affiliates. These assets end up on the books of AGL and/or the other applicable affiliates. When the asset serves as a benefit to all Southern Company Gas affiliates, the asset is recorded on the books of ASC and remains there. AGL's portion of these ASC plant asset costs are then allocated to AGL as part of the ratemaking process.

- ASC direct assigned, or pushed down, at least $101.237 million in plant assets to AGL as of the end of 2018. From 2019 through 2023, an additional $45.299 million in ASC originated information technology asset costs were added to AGL's plant in service due to the push down of such costs. The costs pushed down to AGL during the last four years alone represent almost half of the amount pushed down in all years previous to 2019 combined.

- ASC and AGL implemented a methodology and accounting change related to the direct assigned plant assets in August 2022 in conjunction with its Enterprise Foundations ("Enterprise") software. Contemporaneous with the implementation of Enterprise, ASC began to direct assign the CWIP each month to AGL for book accounting purposes and discontinued the addition of AFUDC on its own accounting books during the construction period. On certain CWIP projects that ASC still retains and does not direct assign to AGL, ASC continues to add AFUDC to the CWIP balance and continues to allocate this CWIP to AGL solely for ratemaking purposes. The authorized grossed-up rate of return is applied to each set of plant assets for ratemaking purposes.

- AGL includes AFUDC on any CWIP directly recorded on its accounting books, which, when grossed up for income taxes, offsets and reduces the effect of the grossed-up return on CWIP included in the revenue requirement. Prior to the change in accounting in August 2022, AGL did not include AFUDC in operating income on any of the CWIP that was recorded on ASC's accounting books, whether it would be later direct assigned to AGL or allocated to AGL for ratemaking purposes only. This mistake had the effect of improperly increasing the GRAM and other revenue requirement determinations for AGL. Reflecting the AFUDC in operating income prevents the

double recovery of the return on the CWIP assets in the buildup of CWIP balances and the recovery of the return on the overall CWIP balances for ratemaking purposes. This mistake was corrected in August 2022 with the change in accounting for the CWIP costs incurred by ASC, then direct assigned and recorded on AGL's accounting books each month during construction. However, this mistake has not yet been corrected for the CWIP that is retained on ASC's accounting books, but allocated to AGL solely for ratemaking purposes. The Company acknowledges the mistake and has made a proposal to correct it in future GRAM and other revenue requirement determinations. While a GRAM ratemaking adjustment to incorporate the effects of the AFUDC on operating income is appropriate, the Company's proposed fix does not completely correct the issue.

- Centralized service costs originating at SCS and ASC are charged to AGL and the other Southern Company Gas affiliates based on methodologies contained in their cost allocation manuals and affiliate service agreements. The methodologies used to charge shared service expenses from SCS and ASC to AGL remain largely unchanged compared to those reviewed in the 2019 Affiliate Audit in Docket No. 42315. The Commission deemed those methodologies as reasonable in its Final Order in that proceeding. Thus, Kennedy and Associates makes no additional recommendations regarding the service company methodologies used to charge expenses to AGL.

C. Summary of Recommendations

Kennedy and Associates makes the following recommendation based upon the 2024 Affiliate Audit findings cited in the preceding section. This recommendation is addressed further in a subsequent section of this Audit Report.

- For ASC plant related CWIP allocated to AGL for ratemaking purposes, the Commission should require AGL to include AFUDC in operating income based on AGL's after-tax full rate of return, similar to the actual AFUDC operating income adjustments related to AGL-owned CWIP assets in the GRAM model. When this AFUDC is grossed-up as a component of and offset to the operating income deficiency, the resulting revenue requirement effect will offset the revenue requirement calculated on the ASC CWIP pushed down and included in AGL's rate base. This ensures that there is no AGL net revenue requirement on ASC CWIP that already earns AFUDC on ASC's accounting books.

D. Overview of Affiliate Transactions and Costs That Are Charged to AGL

The last formal review of AGL's affiliate transactions occurred in Docket No. 42315, culminating with the Staff filing a 2019 Affiliate Audit Report attached to the September 20, 2019 Panel Testimony of Tony Wackerly and Lane Kollen as PIA Staff Exhibit___(WK-18). That review covered affiliate costs charged to AGL for the years 2016 through 2018. There have been a number of significant developments in the Southern Company and Southern Company Gas affiliate structures and the scope of affiliate transactions since that time primarily due to the Southern Company acquisition of AGLR in July 2016, the Southern Company divestiture of Gulf Power Company on January 3, 2019, the Southern Company Gas divestiture of several gas utilities in 2018, including Elizabethtown Gas Company, Elkton Gas Services, and Florida City Gas, the Southern Company Gas divestiture of Sequent Energy Management, LP on July 1, 2021, and significant increases in the total costs incurred at SCS and ASC and the assignment and/or allocation of those increased costs to AGL. All else equal, these divestitures equate to a higher level of costs being driven down to AGL since there are fewer affiliates receiving services from SCS and ASC.

Prior to the Southern Company acquisition of AGLR, ASC served as the only centralized service provider to the AGLR affiliates. This acquisition added another level of affiliate charges to AGL that were not offset by reductions in affiliate charges to AGL from ASC after the acquisition. SCS, the primary centralized service provider for the Southern Company affiliates, began providing services to the former AGLR affiliates starting in 2016 after the merger was finalized. Subsequent to the merger, Southern Company Gas replaced AGLR as the new holding company for the gas related affiliates. SCS costs are direct charged, direct assigned, and allocated to the Southern Company first tier affiliates, including Southern Company Gas, on a monthly basis. The charges

from SCS to Southern Company Gas are combined with the costs incurred directly by ASC and then are direct charged, direct assigned, and allocated to AGL and the other Southern Company Gas affiliates by ASC utilizing ASC methodologies. With the exceptions of the ASC and AGL accounting for direct assigned plant assets, including the calculations of allowance for funds used during construction ("AFUDC") at ASC and AGL, the SCS and ASC cost assignment and allocation methodologies remain largely unchanged since the last affiliate review.

SCS charges Southern Company Gas for expense and capital costs and ASC on behalf of Southern Company Gas charges AGL and other Southern Company Gas affiliate for expense and capital costs. The expensed costs charged by SCS and ASC to AGL have increased significantly since the Southern Company acquisition of AGLR in July 2016. The table below provides expensed cost data from Staff's last audit report and consists of expensed charges to AGL for the years 2016 through 2018 for expenses originating at both centralized service companies, SCS and ASC. Expense charges to AGL increased from $65.006 million in 2016 to $80.130 million in 2018 as shown on the following table, primarily due to increases in total SCS and ASC O&M and A&G expenses.

AGL Affiliate Expense Charges from Both Service Companies By Year
$

	2016	2017	2018
SCS Direct Charged	-	-	-
SCS Direct Assigned	16,882	476,362	5,083,924
SCS Allocated	1,555,570	5,050,176	19,300,934
Total SCS Costs	1,572,452	5,526,538	24,384,858
ASC Direct Charged	9,351,458	11,763,539	3,933,613
ASC Direct Assigned	12,453,607	12,042,992	11,854,019
ASC Allocated	41,628,037	39,828,767	39,957,785
Total ASC Costs	63,433,102	63,635,298	55,745,417
Total - All	65,005,555	69,161,835	80,130,275
O&M and A&G	58,811,876	61,907,309	72,641,569
Depreciation	4,137,059	5,073,707	5,652,636
Other Taxes	1,999,055	1,964,723	1,780,522
All Other	57,566	216,096	55,549
Total - All By Category	65,005,555	69,161,835	80,130,275

SCS and ASC expense charges to AGL increased even more significantly in the years 2019 through 2023, as shown in the following table. The annual expense charges more than doubled from $65.006 million incurred in 2016 to $132.343 million incurred in 2023, an increase of nearly 104%.

AGL Affiliate Expense Charges from Both Service Companies By Year
$

	2019	2020	2021	2022	2023
SCS Direct Charged	-	-	-	239,356	435,711
SCS Direct Assigned	5,092,882	4,677,328	5,311,038	4,354,844	4,614,650
SCS Allocated	25,818,453	27,358,768	27,229,128	37,389,152	39,410,492
Total SCS Costs	30,911,335	32,036,096	32,540,166	41,983,352	44,460,853
ASC Direct Charged	1,378,392	2,288,561	2,860,362	5,916,253	9,257,995
ASC Direct Assigned	12,457,113	11,739,405	10,988,644	11,810,761	14,885,923
ASC Allocated	40,752,291	44,537,020	52,355,646	60,507,406	63,738,638
Total ASC Costs	54,587,796	58,564,986	66,204,653	78,234,419	87,882,556
Total - All	85,499,132	90,601,082	98,744,818	120,217,771	132,343,410
O&M and A&G	78,112,945	81,982,890	89,161,950	108,102,736	117,284,961
Depreciation	5,575,498	6,320,741	7,383,935	8,966,490	10,162,457
Other Taxes	1,736,431	2,113,568	2,185,765	3,121,658	4,832,611
All Other	74,258	183,883	13,168	26,887	63,381
Total - All By Category	85,499,132	90,601,082	98,744,818	120,217,771	132,343,410

The data shows that the largest dollar and percentage increases in SCS and ASC expense charges to AGL since 2018 occurred in 2022. Expense charges increased from $98.745 million in 2021 to $120.218 million in 2022, an increase of $21.473 million (21.7%) in a single year. Expense charges from SCS experienced relatively minimal increases from 2019 to 2021, increasing from $30.911 million in 2019 to $32.540 million in 2021. However, expense charges from SCS increased from $32.540 million in 2021 to $41.983 million in 2022, an increase of $9.443 million (29.0%) in one year. Expense charges originating at ASC grew more consistently throughout the years 2019 through 2023, but they grew at a more rapid rate in 2022 from $66.205 million in 2021

to $78.234 million in 2022. This amounted to an increase in charged expenses originating at ASC to AGL of $12.029 million (18.2%) in a single year.

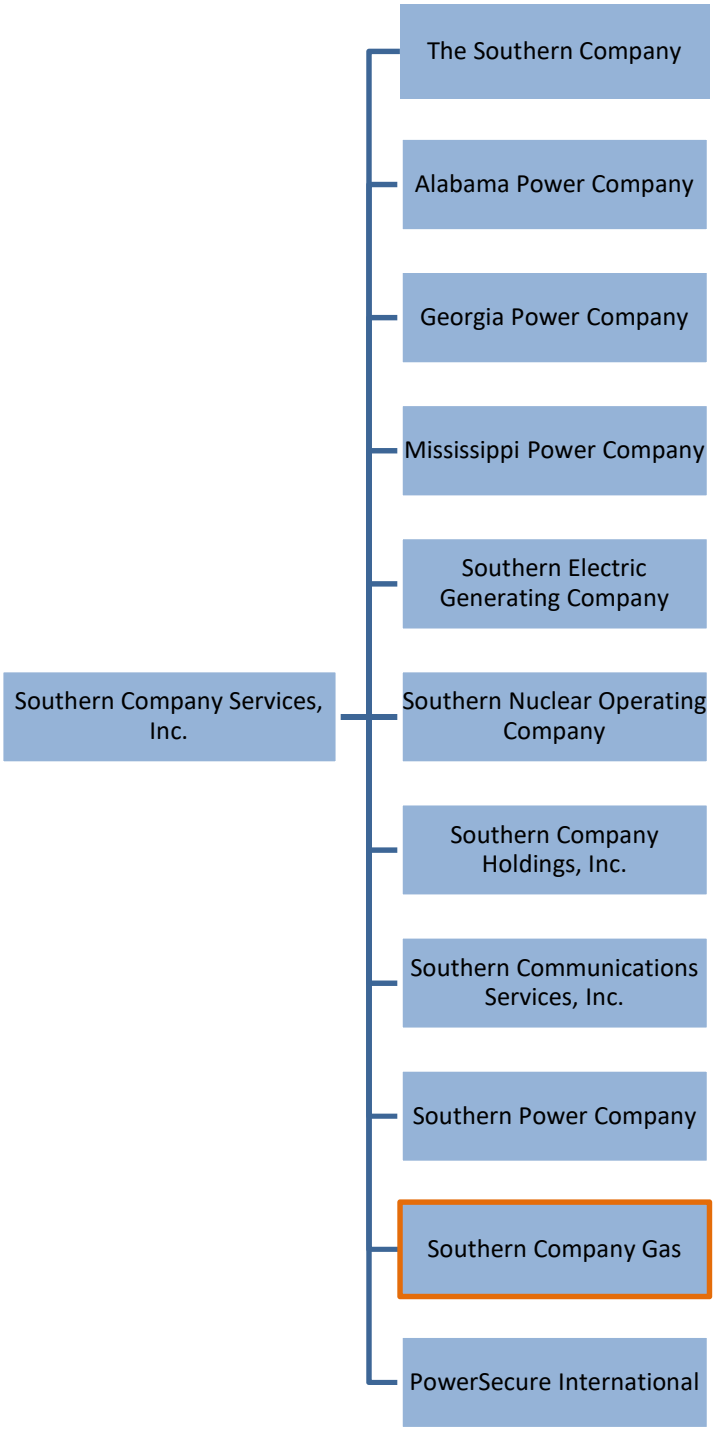
Capital charges have also grown significantly in recent years. Plant assets assigned directly to AGL by ASC on a cumulative basis for all previous years amounted to $101.237 million as of the end of 2018.[1] Plant assets assigned directly to AGL by ASC for only the four years 2019 through 2023 amounted to $45.299 million, almost half of the amount directly assigned to AGL in all previous years combined.

E. Summary of AGL Affiliate Relationships

The two charts below depict the primary affiliates receiving services from both SCS and Southern Company Gas via ASC. The first chart shows the primary affiliates that were receiving services from SCS as of the end of 2023. Gulf Power Company was sold to NextEra Energy effective January 3, 2019, so it no longer receives such services. Costs are first charged to these affiliates and then driven further in some cases to their other affiliates downstream. Southern Company Gas is highlighted in the chart since those charges directly affect charges eventually made to AGL.

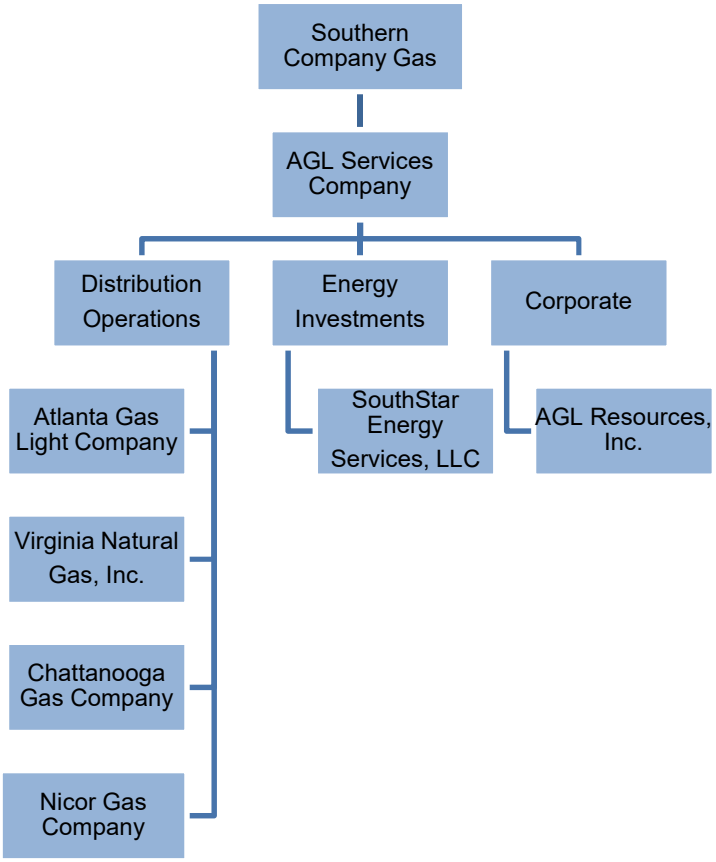
[1] AGL's response to STF-10-30. AGL was unable to provide the annual capital charges in each year prior to 2019 in response to PIA Staff discovery.

Southern Company Services, Inc.
Primary Affiliates Organizational Chart



The primary Southern Company Gas affiliates receiving services from ASC as of the end of 2023 are summarized in the chart below. The chart does not reflect the former Southern Company Gas wholesale services affiliate, Sequent Energy Management, LP, since it was divested in 2021.

Southern Company Gas
Primary Affiliates Organizational Chart



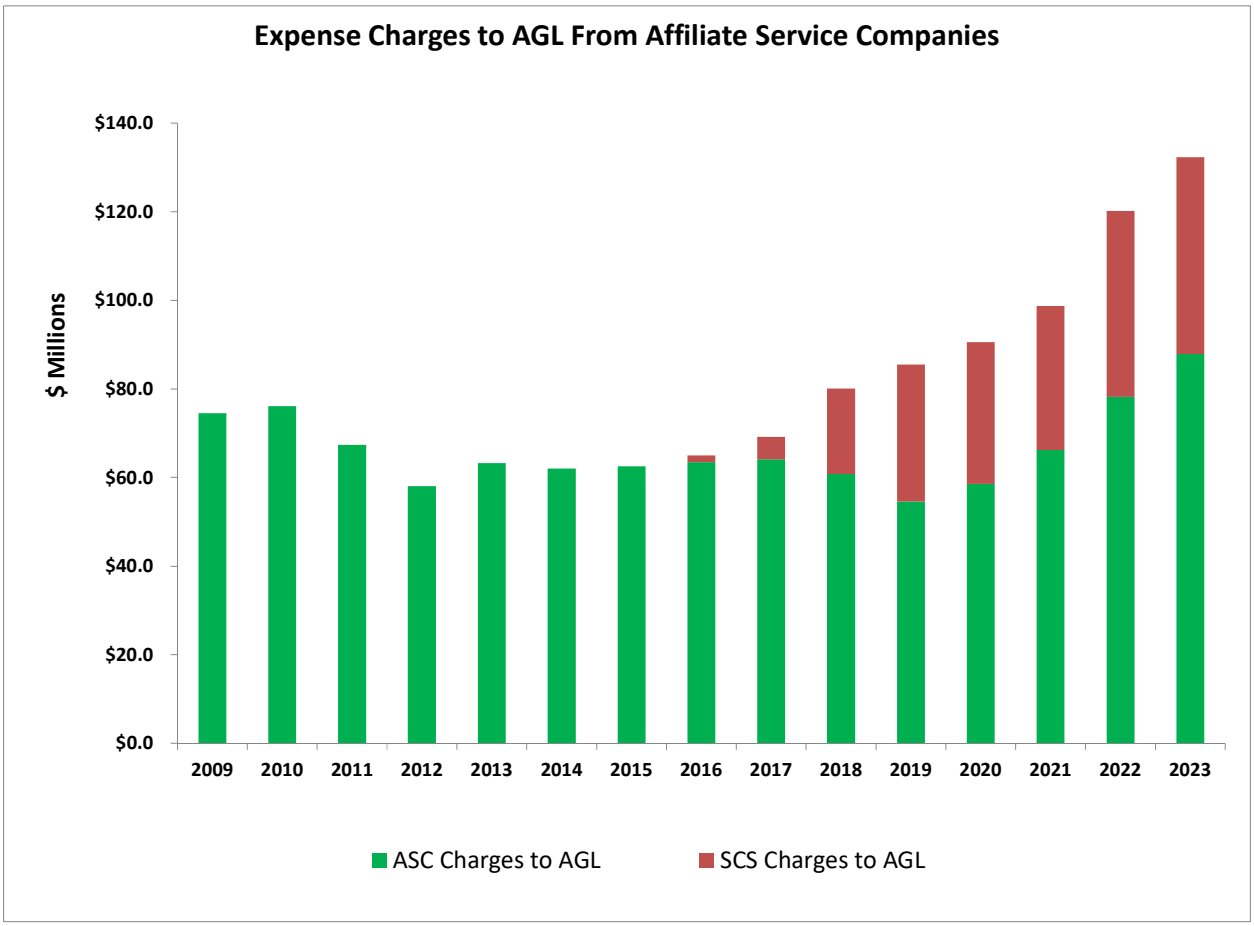
Southern Company Gas is an energy services holding company for numerous companies, including four gas distribution companies, AGL, Virginia Natural Gas, Inc., Chattanooga Gas Company, and Nicor Gas Company; ASC; Southstar Energy Services, LLC, doing-business-as Georgia Natural Gas, a nonregulated gas supplier within the AGL service territory doing business as

Georgia Natural Gas; and AGLR. ASC made charges to numerous other affiliates of Southern Company Gas during the review period, but the affiliates portrayed in the chart above receive over 90% of all ASC charges made.

F. History of Affiliate Service Company Expenses Charged to AGL

AGL achieved annual net merger synergy savings of $10.839 million from the 2011 merger of AGLR and Nicor due to the service company consolidation of duplicate activities and functions and adoption of best practices. These savings were quantified on behalf of AGL by Concentric Energy Advisors, Inc. and detailed in a December 2013 report filed in Docket No. 31647-U.

In contrast to the merger of AGLR with Nicor, the Southern Company acquisition of AGLR has not resulted in lower service company charges and savings to AGL. In fact, service company expense charges to AGL have increased significantly since 2015, the full calendar year just prior to the acquisition. AGL's service company expense charges have increased from $62.521 million in 2015 to $132.343 million in 2023, an increase of 111.7% in only eight years. These increases have been driven in large part by increases in full-time equivalent employees ("FTEs") employed at the service companies. There has been an increase in ASC FTEs since the beginning of 2019 of 159, an increase of 15.7%. There has also been an increase in SCS FTEs since the beginning of 2019 of 464, an increase of 12.3%. The following graph shows the expense charges from both the service company providers to AGL since 2009. It shows the decrease in costs following the Nicor merger and the increases in costs following the acquisition of AGLR by Southern Company.


Expense Charges to AGL From Affiliate Service Companies
$ Millions
$140.0
$120.0
$100.0
$80.0
$60.0
$40.0
$20.0
$0.0
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018
2019
2020
2021
2022
2023
ASC Charges to AGL
SCS Charges to AGL

II. AFFILIATE TRANSACTIONS AND COSTS CHARGED TO AGL

A. SCS Charges to Affiliates

The first set of centralized service affiliate charges affecting AGL originates at SCS. Centralized services consist of services obtained from third parties by SCS and the internal costs of SCS, including payroll, benefits, and other overhead costs. While SCS currently performs centralized services at cost predominately for Southern Company's electric-related affiliates, it also charges certain corporate-level services to Southern Company Gas through the SCS-ASC Services Agreement. These charges are governed by the SCS cost allocation manual ("CAM") specifically named the Cost Accountability and Control Manual, which was last updated in 2023.[2] ASC in turn charges costs generated at SCS among its affiliates according to various service agreements including the ASC-AGL Services Agreement that has been in place since 2008 as well as the ASC CAM. The charge methodologies for the SCS-generated costs match those used to charge all other ASC costs to its affiliates. However, no gas supply and capacity management costs are currently generated at SCS, so none of those types of costs are charged to AGL through this process.

The table below shows the SCS total costs charged to all its first tier affiliates, such as Southern Company Gas, for each of the years 2019 through 2022 based on FERC Form 60 data available at the time of this report as provided in discovery. As is the case for the Southern Company Gas affiliates, these charges are added to the costs incurred by ASC and then charged to second tier affiliates. The table shows an increasing level of total costs charged to Southern

[2] AGL's Response to STF-10-3.

Company Gas, which in turn get charged to its affiliates that include AGL by way of ASC. The table also shows that total ASC charges and charges to Southern Company Gas were relatively constant during 2020 and 2021 but rose significantly in 2022. Southern Company Gas's percentage of overall SCS charged costs remained relatively constant at around 12.4% for each year 2020 through 2022.

Southern Company Services, Inc.
Total Costs Charged to Each Affiliate
Based on FERC Form 60 Data (Page 307)

	2019		2020		2021		2022	
Affiliate Company	Amount $	%	Amount $	%	Amount $	%	Amount $	%
The Southern Company	121,160,121	6.3%	104,965,361	5.5%	108,842,647	5.6%	134,663,614	6.4%
Alabama Power Company	527,221,480	27.5%	478,241,961	25.0%	503,744,582	25.9%	548,562,398	26.1%
Georgia Power Company	703,829,625	36.7%	638,996,301	33.4%	662,988,379	34.1%	761,901,591	36.2%
Mississippi Power Company	118,484,848	6.2%	148,601,241	7.8%	119,605,413	6.2%	114,580,154	5.4%
Southern Electric Generating Company	5,006,695	0.3%	5,093,796	0.3%	4,187,340	0.2%	1,552,843	0.1%
Southern Nuclear Operating Company	102,255,559	5.3%	134,919,211	7.0%	132,991,224	6.8%	115,172,052	5.5%
Southern Company Holdings, Inc.	38,906,821	2.0%	43,149,854	2.3%	48,007,373	2.5%	44,490,789	2.1%
Southern Communications Services, Inc.	12,599,656	0.7%	21,024,263	1.1%	23,065,985	1.2%	20,655,538	1.0%
Southern Power Company	89,682,834	4.7%	87,416,117	4.6%	88,918,101	4.6%	86,085,467	4.1%
Southern Company Gas	**183,371,087**	**9.6%**	**236,726,433**	12.4%	**239,324,975**	12.3%	**261,589,224**	12.4%
PowerSecure International	16,042,559	0.8%	15,972,521	0.8%	12,997,024	0.7%	13,209,460	0.6%
Total	1,918,561,285	100.0%	1,915,107,059	100.0%	1,944,673,043	100.0%	2,102,463,130	100.0%

The costs in the preceding table represent total costs charged by SCS to each affiliate, including all capitalized construction costs. These SCS affiliates were also portrayed on the chart in the Executive Summary of this Report.

Since the primary focus of this affiliate review is on the various types of costs driven down to AGL, Kennedy and Associates broke down the total SCS costs further into cost categories using more detailed account data in the FERC Form 60 filed each year. The table

below shows that O&M expenses that are charged only to electric utilities have been decreasing, while A&G expenses that are charged to all affiliates have been increasing. That is an especially concerning fact given that SCS-generated costs charged in the end to AGL have been experiencing large increases as shown in the table in the Executive Summary. A&G costs originating at SCS and eventually charged to AGL amounted to $30.911 million in 2019, $32.036 million in 2020, $32.540 million in 2021, growing significantly to $41.983 million in 2022, and growing further to $44.461 million in 2023.

Southern Company Services, Inc.
Total Costs Charged to Affiliates by Category
Based on FERC Form 60 Data (Pages 303-307)
$

	2019	2020	2021	2022
O&M Expense - Electric	266,121,925	251,105,258	264,202,825	238,983,189
A&G Expense	838,293,096	821,441,618	912,905,376	1,002,594,875
Depreciation Expense	16,681,909	16,986,733	16,931,073	8,809,945
Amortization Expense				29,128,396
Other Taxes	40,190,072	34,474,948	40,100,253	32,372,536
Net Income Taxes	(6,012,946)	12,917,439	5,593,840	2,816,518
Construction or Other Services	740,557,968	757,274,433	678,659,947	744,626,227
Merchandising, Jobbing, and Contract Work	2,515,053	3,665,406	5,018,387	4,801,029
Below the Line Items	20,214,208	17,241,224	21,261,342	38,330,415
Total All With Construction	1,918,561,285	1,915,107,059	1,944,673,043	2,102,463,130
Total All Without Construction	1,178,003,317	1,157,832,626	1,266,013,096	1,357,836,903
Total O&M and A&G	1,104,415,021	1,072,546,876	1,177,108,201	1,241,578,064

A&G Includes Customer Service and Sales Accounts 901-916

B. ASC Charges to Affiliates

During the 2019 – 2023 review period, ASC provided centralized services to AGL and the other Southern Company Gas affiliates. All costs of ASC are charged monthly to the various Southern Company Gas affiliates, primarily to the four gas distribution companies and Southern Company Gas (AGLR). Southern Company Gas is charged and retains certain costs, including costs that cannot be recovered by the gas distribution companies through the ratemaking process. Over 90% of the total ASC costs were being charged to the four gas distribution companies and Southern Company Gas, depicted in the chart in the Executive Summary section of this report, at the end of 2023.

The following table summarizes the expenses charged by ASC to its affiliates during the review period broken out between those costs originating at SCS and those originating at ASC.[3]

[3] The Data sources for the table are the quarterly and annual reporting affiliate and GRAM reporting supplemented with the response to STF-17-4.

ASC Expense Charges to Affiliates and Portion Charged to AGL
Charges Sourced from Both Service Companies By Year
$

	2019	2020	2021	2022	2023
Costs Originating at SCS and Charged to ASC					
SCS Direct Charges	-	-	-	[redacted]	[redacted]
SCS Direct Assigned Charges	24,862,812	24,224,778	21,119,467		
SCS Allocated Charges	86,477,922	92,348,429	96,082,451		
Total Costs Originating at SCS	111,340,734	116,573,207	117,201,918	[redacted]	[redacted]
Costs Originating at ASC					
ASC Direct Charges	4,384,343	7,764,719	9,513,754	[redacted]	[redacted]
ASC Direct Assigned Charges	29,816,473	30,005,677	25,741,170		
ASC Allocated Charges	136,957,898	150,334,408	159,750,482		
Total Costs Originating at ASC	171,158,714	188,104,804	195,005,406	[redacted]	[redacted]
Total ASC Charges to Affiliates	282,499,448	304,678,011	312,207,324	[redacted]	[redacted]
ASC Charges to AGL					
Direct Charges	1,378,392	2,288,561	2,860,362	6,155,609	9,693,706
Direct Assigned Charges	17,549,995	16,416,733	16,299,682	16,165,604	19,500,573
Allocated Charges	66,570,744	71,895,788	79,584,773	97,896,558	103,149,130
Total - ASC Charges to AGL	85,499,132	90,601,082	98,744,818	120,217,771	132,343,410
AGL % of Total ASC Charges	30.3%	29.7%	31.6%	[redacted]	[redacted]

Note: The Company affiliate reports for 2022 did not provide a split of the SCS charges by charge category.

ASC, on behalf of Southern Company Gas, charged an increasing amount in centralized services expenses to its affiliates from 2019 to 2023, ranging from $282.499 million in 2019 to [redacted] million in 2023. Those costs were sourced from both its own incurred costs as well as the costs originally incurred at SCS and then charged to Southern Company Gas. AGL's portion of ASC charges ranged from 29.7% to [redacted] during those years. The data shows that service company charges to AGL have increased significantly from 2019 to 2023, from $85.499 million to $132.343 million.

The increase in expense charges from both service companies that were eventually charged by ASC to AGL are driven by two factors as shown in the table above. First, overall service company expenses increased dramatically over this period, especially in 2022. 2022 expenses originating at SCS charged to all Southern Company Gas affiliates increased by [redacted] in 2022 alone. 2022 expenses originating at ASC charged to all Southern Company Gas affiliates increased by [redacted] in 2022 alone. This combined for an increase in 2022 expenses charged to all Southern Company Gas affiliates of [redacted]. Second, the percentage of expenses charged to AGL compared to expenses charged to all Southern Company Gas affiliates also reflected increases. Overall charges to AGL as a percentage of charges from ASC to all Southern Company Gas affiliates amounted to an average of 26.2% for the years 2016 through 2018 as reflected in PIA Staff's 2019 Affiliate Audit Report. That percentage increased in 2019 and 2020 to around 30% on average, primarily as a result of the divestures of Elizabethtown Gas Company, Elkton Gas Services, and Florida City Gas in the latter part of 2018 without a concomitant reduction in ASC costs to provide services to fewer affiliates. AGL's percentage of total service company expense charges began growing in 2021 to 31.6% and increased to [redacted]% in 2022 and to [redacted]% in 2023.

There are two primary causes of the increased costs and percentage of costs charged to AGL since 2020. First, Sequent Energy Management, LP, a non-regulated company, was divested on July 1, 2021. Thus, a substantial amount of ASC expense charges starting in July 2021 had to be charged to the remaining companies receiving services after the divestiture. Second, [redacted]

[redacted]

[redacted]

C. Full-Time Equivalent Employees ("FTEs") at the Service Companies

There have been significant increases in the number of service company FTEs since the beginning of the audit period and they continue to grow at alarming rates. Adding to the concern is that the FTE levels are growing so much considering the Southern Company and Southern Company Gas divestitures as noted above. These increases represent another important factor in the significant increases in affiliate charges to AGL. The Company provided the number of FTEs at each of the service companies during the audit review period in response to discovery.[4] The table below summarizes the FTEs at the end of each year. There were 1,014 FTEs at ASC at the beginning of 2019. That number grew to 1,150 as of the end of 2023 and to 1,174 as of the last reported date of February 21, 2024. That represents a growth of 159 FTEs from January 1, 2019 until February 21, 2024, an increase of 15.7%. There were 3,760 FTEs at SCS at the beginning of 2019. That number grew to 4,205 as of the end of 2023 and to 4,224 as of February 21, 2024. That represents a growth of 464 FTEs from January 1, 2019 until February 21, 2024, an increase of 12.3%. Overall, the combined ASC and SCS increase in the number of FTEs was 13.0% during this period.

[4] AGL's response to STF-10-24.

Summary by Year - Service Company FTEs
Source Attachment STF-10-24
End of Each Year

	FTEs	Increase	Incr %	Total Increase	Total Incr %
ASC					
12/31/2018	1,014				
12/31/2019	1,071	57	5.6%		
12/31/2020	1,110	39	3.6%		
12/31/2021	1,052	(58)	-5.2%		
12/31/2022	1,111	59	5.6%		
12/31/2023	1,150	39	3.5%		
2/21/2024	1,173	23	2.0%	159	15.7%
SCS					
12/31/2018	3,760				
12/31/2019	3,697	(63)	-1.7%		
12/31/2020	3,771	74	2.0%		
12/31/2021	3,845	74	2.0%		
12/31/2022	4,046	201	5.2%		
12/31/2023	4,205	159	3.9%		
2/21/2024	4,224	19	0.5%	464	12.3%
Total					
12/31/2018	4,774				
12/31/2019	4,768	(6)	-0.1%		
12/31/2020	4,881	113	2.4%		
12/31/2021	4,897	16	0.3%		
12/31/2022	5,157	260	5.3%		
12/31/2023	5,355	198	3.8%		
2/21/2024	5,397	42	0.8%	623	13.0%

D. Capitalized (Shared Plant Asset) Cost Charges

Construction (capital) costs are incurred by SCS and ASC on behalf of AGL, and the other Southern Company Gas affiliates, and are either direct assigned to AGL or allocated to AGL for ratemaking purposes only. These plant asset costs are mostly technology based but also include other classes of general plant, such as facilities, furniture, and fixtures.[5] Assets are direct assigned, or pushed down, to specific ASC affiliates when they benefit those specific affiliates. These assets end up on the books of AGL and/or the other applicable affiliates. We refer to these assigned plant asset costs on AGL's accounting books as ASC Embedded Plant to distinguish them from assigned expense costs. When the asset serves as a benefit to all Southern Company Gas affiliates, the asset is recorded on the books of ASC and remains there. This recording difference defines the way each type of costs is treated in rate base for rate recovery purposes. AGL includes the ASC Embedded Plant costs for cost recovery purposes in rate base as plant in service assets owned by AGL. AGL performs a proforma adjustment related to the ASC-owned asset costs so that the allocated portions of those plant-related costs are also included as a component of AGL's rate base. For cost recovery purposes, the Company's ratemaking proforma adjustment not only includes plant in service, but it also includes an allocation of associated construction work in progress ("CWIP"), accumulated depreciation, and accumulated deferred income taxes ("ADIT") so that the allocated portions of these plant-related costs are also included as a component of AGL's rate base. In this way, AGL receives a full rate of return on these ASC allocated costs as if they are owned and financed by AGL. AGL has long held the

[5] Direct Testimony of Michael J. Morley at 7.

opinion that these ASC allocated costs should receive AGL's authorized full rate of return the same as if they had been reflected on the accounting books of AGL, no matter how the costs were financed by ASC.

Prior reporting in AGL ratemaking proceedings and in quarterly filed GRAM and affiliate reports did not provide information detailing these ASC Embedded Plant costs that had been assigned to AGL over the years. Previously, such affiliate reporting and discovery response reporting had been limited to expense charges from each of the service companies to AGL. In response to the Commission Staff's concerns about this lack of reporting, the Company has agreed to provide additional information in regards to the ASC Embedded Plant costs in its quarterly and annual reporting and in ratemaking proceedings. This is evident from the detailed description of such costs that were provided in the Direct Testimony of Mr. Morley in this proceeding, Docket No. 43820.

Kennedy and Associates was able to confirm that ASC had direct assigned, or pushed down, these ASC Embedded Plant costs to AGL for accounting and ratemaking purposes in prior years. In response to discovery, AGL quantified at least $101.237 million in such information technology hardware and software costs that had been pushed down from ASC and that was recorded on the accounting books of AGL as of the end of 2018.[6] AGL also provided a copy of a data response from the 2019 rate case, Docket No. 42315, which included a brief description of a portion of these costs and how they were reflected in the Company's revenue requirement

[6] AGL's response to Staff 10-30, Attachment STF-10-30a.

determination.[7] From 2019 through 2023, an additional $45.299 million in ASC Embedded Plant costs has been added to AGL's plant in service due to the push down of such costs.[8]

ASC and AGL implemented a methodology and accounting change related to the direct assigned plant assets in August 2022 in conjunction with the implementation of new accounting procedures at the same time that Southern Company implemented the Enterprise Foundations ("Enterprise") software. Prior to the implementation of Enterprise, ASC retained CWIP incurred for its affiliates on its accounting books during the construction period, where ASC added allowance for funds used during construction ("AFUDC") calculated at its cost of debt to CWIP. ASC allocated the CWIP, including the AFUDC that was recorded on its accounting books, to AGL solely for ratemaking purposes during the construction period. AGL included this ASC CWIP in its rate base. Contemporaneous with the implementation of Enterprise, ASC direct assigned the CWIP each month to AGL for book accounting purposes and discontinued the addition of AFUDC on its accounting books. On certain CWIP projects that ASC still retains and does not direct assign to AGL, ASC continues to add AFUDC to the CWIP balance and continues to allocate this CWIP to AGL solely for ratemaking purposes.

AGL included and continues to include its own directly incurred CWIP, the ASC capital charges direct assigned and recorded to CWIP on AGL's accounting books since the implementation of Enterprise, and the ASC capital charges allocated to AGL solely for ratemaking purposes in its rate base, including the SRR and GRAM rate base calculations, where the grossed-up return on those rate base investments is included in the revenue requirement.

[7] AGL's response to Staff 10-11, including attachments.
[8] AGL's response to STF-10-30, Attachment STF-10-30e.

AGL continues to include AFUDC on its own directly incurred CWIP and now, since the accounting changes implemented contemporaneously with Enterprise, includes AFUDC on the ASC CWIP recorded on AGL's accounting in operating income, which, when grossed up for income taxes, offsets and reduces the effect of the grossed-up return included in the revenue requirement.

Prior to the change in accounting in August 2022, AGL did not include AFUDC in operating income on any of the CWIP that was recorded on ASC's accounting books, whether it would be later direct assigned to AGL or allocated to AGL for ratemaking purposes only. This mistake had the effect of improperly increasing the GRAM and other revenue requirement determinations for AGL. Reflecting the AFUDC in operating income prevents the double recovery of the return on the CWIP assets in the buildup of CWIP balances and the recovery of the return on the overall CWIP balances for ratemaking purposes. The Company corrected this mistake in August 2022 with the change in accounting for the CWIP costs incurred by ASC, then direct assigned and recorded on AGL's accounting books each month during construction. The Company has not yet corrected this mistake for the CWIP that is retained on ASC's accounting books, but allocated to AGL solely for ratemaking purposes. The Company agreed it was necessary to correct this remaining mistake and proposed a fix that it would implement in the 2025 GRAM filing and reflect in other future rate case filings that require the calculation of AGL's revenue requirement. In response to discovery, AGL made the following statement and proposal.[9]

AGL currently does not include an operating income adjustment for ratemaking purposes

[9] AGL's response to STF-17-2.

for capitalized interest on ASC allocable shared assets. In future GRAM filings, rate case proceedings, and other filings that require the calculation of AGL's revenue requirement, the Company will include a ratemaking adjustment to incorporate AGL's portion of the capitalized interest on ASC allocable shared assets.

While a GRAM ratemaking adjustment to incorporate the effects of the AFUDC on operating income is appropriate, the Company's proposed fix does not completely correct the issue. The return on the CWIP assets allocated to AGL for ratemaking purposes is computed based upon AGL's fully grossed-up rate of return applicable to 100% of the CWIP assets, not just the debt rate applicable to ASC as the response seems to indicate. The ratemaking adjustment to reflect the ASC AFUDC as additional operating income does not fully offset the return on the CWIP balances included in the revenue requirement.

Kennedy and Associates makes the following recommendation:

- For ASC plant related CWIP allocated to AGL for ratemaking purposes, the Commission should require AGL to include AFUDC in operating income based on AGL's after-tax full rate of return, similar to the actual AFUDC operating income adjustments related to AGL-owned CWIP assets in the GRAM model. When this AFUDC is grossed-up as a component of and offset to the operating income deficiency, the resulting revenue requirement effect will offset the revenue requirement calculated on the ASC CWIP pushed down and included in AGL's rate base. This ensures that there is no AGL net revenue requirement on ASC CWIP that already earns AFUDC on ASC's accounting books.

E. Recent Changes in SCS and ASC Affiliate Structures and Effects on Charges to Remaining Affiliates

The two charts in the Executive Summary section of this report portray the primary affiliates receiving services from both SCS and Southern Company Gas via ASC as of the end of 2023. The first chart shows the primary affiliates that were receiving services from SCS as of the end of 2023. Gulf Power Company was sold to NextEra Energy effective January 3, 2019, so it no longer

receives such services. All else equal, costs charged by SCS to Southern Company Gas, and then from ASC to AGL, have increased due to one fewer affiliate in which to spread costs.

The affiliate chart for ASC in the Executive Summary does not reflect the former Southern Company Gas affiliates who received services from ASC on behalf of Southern Company Gas up until their divestitures in 2018, including Elizabethtown Gas Company, Elkton Gas Services, Florida City Gas, Nicor Home Services, and Nicor Services. In addition, Southern Company Gas divested Sequent Energy Management, LP on July 1, 2021. All else equal, Southern Company Gas costs charged by ASC to AGL have increased due to fewer affiliates in which to spread costs.

F. Description of SCS Allocation Methodologies and Expense Charges to Southern Company Gas

The SCS FERC Form 60 lists the following business units for which services are provided by SCS to its affiliates:

- Accounting
- Finance and Treasury
- Aerial Services
- Auditing
- Corporate Services
- Environmental and Research
- Executive and Corporate
- External Affairs
- Transmission
- Facilities and Real Estate
- Generation
- Governmental Affairs
- Humans Resources
- Information Technology
- Legal and General Counsel
- Operations
- Shared Services
- Supply Chain Management

The FERC Form 60 and the SCS CAM describe the process for monthly charges made to each of its affiliates. Charges can be condensed into two major classifications, direct and project allocations. Direct charged costs benefit just one affiliate while the project allocation costs are

allocated based on predefined company target pools depending on the group(s) of affiliates receiving the applicable services. The SCS allocation methods can also be found in the FERC Form 60 for each year and in the SCS CAM. The allocation methods as defined in the 2023 CAM are summarized below:

[redacted]

[redacted]

[redacted]

There have been several changes, additions, and deletions to the allocation methodologies in the SCS CAM since the 2019 Affiliate Audit as these methodologies are reviewed as needed. However, most of those changes involve allocations to the various electric utilities. The only allocation methods used to charge allocated costs to Southern Company Gas (for which accumulated costs were then charged to AGL via charges from ASC) at the end of 2023 included the following:[10]

Financial Basis
Employee Basis
Network ID

[10] AGL's response to STF-10-12, Attachment STF-10-12a.

System Air Availability
Total SCS Billings Basis

The Financial Basis allocation method is one utilized to charge a large portion of the SCS expense charges to Southern Company Gas for eventual charges to AGL. While the current SCS Financial Basis Ratio has changed somewhat since the 2019 Affiliate Audit, it is currently a composite rate based upon [redacted]. It is based on [redacted].

G. Description of ASC Allocation Methodologies and Expense Charges to AGL

The ASC CAM lists the following services currently provided by ASC to its affiliates:

- Rates and Regulatory
- Internal Auditing
- Gas Supply, Capacity Planning and Management
- Engineering Services
- Financial Services
- Information Systems
- Strategic Planning
- Business Support[11]
- Other
- Customer Services
- Employee Services
- Marketing
- Legal Services and Risk Management
- Executive
- External Relations
- Corporate Communications
- Corporate Compliance and Secretary

This list of services is slightly expanded compared to the list of services depicted in the ASC-AGL Services Agreement.[12] The ASC-AGL Services Agreement serves as another procedures manual in addition to the CAM detailing the affiliate charge process including how costs are allocated to affiliates.

[11] Business Support includes Purchasing, Facilities Management and Fleet.
[12] A copy of the agreement was provided in AGL's response to STF-10-27, Attachment A.

The costs of the ASC centralized services are incurred by the Southern Company Gas affiliates through the affiliate transaction process, which is a structured process of charging and billing from one Southern Company Gas affiliate (service provider) to another Southern Company Gas affiliate (service receiver), usually on the basis of some measure of cost. The service provider collects its costs in the form of various cost pools, also known as work orders, the sum of which are the expense and capital costs incurred on behalf of all affiliates. The costs collected in the work orders are charged out to the affiliates based on various measures of cost causation. The service provider recognizes a reduction to expenses for the costs charged and billed to the service receiver and the service receiver recognizes an increase to expenses, which are added to the expenses incurred directly by the service receiver to quantify the affiliate's total expenses.

The costs of providing centralized services are charged from ASC to the various Southern Company Gas affiliates through a "chargeback" process, consisting of direct charges, direct assignments, and allocations. The direct charges are for costs incurred by ASC directly on behalf of an affiliate. The direct assignments are for costs of services provided to specific affiliates and charged to those affiliates based upon time reporting. The allocations are for the costs of services that are provided to multiple affiliates and charged to those affiliates based upon various factors such as full time equivalent employees, end use customers, and a composite ratio based upon other factors, including operating expenses. Other costs also are allocated to the Southern Company Gas affiliates, including income taxes, which are determined on a consolidated basis, and financing costs.

The 2023 ASC CAM summarizes the ASC-AGL Services Agreement allocation methodologies as follows:

Direct Charge
Costs accumulated in specific O&M projects will be directly charged to one or more Southern Company Gas Companies as defined by the project owner. Costs will also be directly charged to Southern Company Gas System Companies using methods determined on a case-by-case basis consistent with the nature of the work performed and/or based on the utilization of one of the standard rates and drivers (Number of Stores Issues Ratio, Rate per Square Foot, Rate per Vehicle, Rate per Computer, Rate per Employee, Direct Charge Payroll, Specific Percentages).

Direct Assigned
Costs accumulated in Account Codes for services specifically performed for one or more Southern Company Gas System Companies are assigned utilizing the unique business unit identifier for all operational costs including payroll expenses. Benefit related expenses will be direct assigned among and charged to such Southern Company Gas System Companies using methods determined on a case- by-case basis consistent with the nature of the work performed and/or based on one of the distribution or allocation methods (Direct Assign Payroll Ratio).

Distributed and Allocated
Costs accumulated in Account Codes for services of a general nature which are applicable to all Southern Company Gas System Companies or to a class or classes of Southern Company Gas System Companies will be allocated among or charged to such Southern Company Gas System Companies by application of one or more of the allocation methods described below.

Number of End-Use Customers Ratio -A ratio based on the number of end-use customers for Southern Company Gas natural gas affiliates. This ratio will be updated at regular intervals, at least annually, using the most recent data reasonably available.

Total Assets Ratio - A ratio based on the total assets less intercompany receivables and intercompany notes. This ratio will be updated at regular intervals, at least annually, using the most recent data reasonably available.

Number of Employees Ratio - A ratio based on the number of employees benefiting from the performance of a service. Additionally, for the parent or holding company of Southern Company Gas, the number of employees are those officers common to the parent and ASC. This ratio will be updated at regular intervals, at least annually, using the most recent data reasonably available.

Call/Phone Volume Ratio - A ratio based on the monthly call volume incurred on behalf of the Southern Company Gas System Companies and may be adjusted for any known and reasonably quantifiable events, or at such time as may be required due to significant changes.

Operating Expense Ratio- A ratio based on total operating expense. This ratio will be updated at regular intervals, at least annually, using the most recent data reasonably

available.

Operating Margin Ratio - A ratio based on operating margin defined as revenue less cost of goods. Additionally, for the parent or holding company of Southern Company Gas, operating margin consists of dividends for the Southern Company Gas System Company subsidiaries. This ratio will be updated at regular intervals, at least annually, using the most recent data reasonably available.

Composite Ratio - This ratio is an average of the above four ratios of: Number of Employees, Total Assets, Operating Expenses and Operating Margin. This ratio will be updated at regular intervals, at least annually, using the most recent data reasonably available.

The following table summarizes the allocation bases utilized by ASC for distributed/allocated charges to the other Southern Company Gas affiliates by departmental service provider as provided in the ASC CAM. As depicted in the table, the vast majority of costs are allocated based on the Composite Ratio.

ASC Distributed/Allocated Drivers

• Rates and Regulatory	Number of End-Use Customers
• Internal Auditing	Composite Ratio
• Strategic Planning	Composite Ratio
• External Relations	Composite Ratio
• Capacity and Gas Supply	Number of End-Use Customers
• Legal Services and Risk Mgmt.	Composite Ratio
• Marketing	Number of End-Use Customers
• Financial Services	Composite Ratio
• Information Systems and Tech.	Composite Ratio
• Executive	Composite Ratio
• Customer Services	Number of End-Use Customers
• Employee Services	Number of Employees
• Engineering	Number of End-Use Customers
• Business Support	
Purchasing	Composite Ratio
Facilities Management	Composite Ratio
Fleet	Composite Ratio
• Corporate Communications	Composite Ratio
• Corporate Compliance & Corporate Secretary	Composite Ratio
• Other	Composite Ratio

Kennedy and Associates reviewed the allocation bases, the selection of Southern Company Gas affiliates included in the allocation (target), the selection of cost or statistical data utilized for the allocation bases, and assessed the use of the various allocation bases against the department costs that were allocated.

Kennedy and Associates concludes that the methodologies used to charge shared service expenses from SCS and ASC to AGL remain largely unchanged compared to those reviewed in the 2019 Affiliate Audit in Docket No. 42315. PIA Staff, including Kennedy and Associates, raised concerns in that proceeding about the selection and utilization of various allocation bases used to charge costs to AGL. The Commission ultimately found that the applicable methodologies were reasonable in its Final Order, which stated the following at page 12:

> "The Commission is not compelled by PIAS's recommendation at this time and finds that AGL's shared service expenses are reasonable and should be included in rates in this proceeding."

Kennedy and Associates makes no additional recommendations regarding the service company methodologies used to charge expenses to AGL.