

**COST OF GAS CLAUSE**

**A. APPLICABILITY**

This Cost of Gas Clause shall apply to all gas sales service rate schedules of Texas Gas Service Company, a Division of ONE Gas, Inc. ("Company") in the following unincorporated areas of its West-North Service Area: Aledo, Breckenridge, Bryson, Graford, Graham, Hudson Oaks, Jacksboro, Jermyn, Millsap, Mineral Wells, Palo Pinto, Perrin, Possum Kingdom, Punkin Center, Weatherford, Whitt and Willow Park, Texas.

**B. DEFINITIONS**

1. Cost of Gas – The rate per billing unit or the total calculation under this clause, consisting of the Commodity Cost, the Customer Rate Relief Component, the Reconciliation Component, any surcharges or refunds, Uncollectible Cost of Gas, and the revenue associated fees and taxes. The Cost of Gas will also include the FERC Intervention Costs.
2. Commodity Cost – The Cost of Purchased Gas multiplied by the Purchase/Sales Ratio plus an adjustment deemed prudent by the Company to correct any known and quantifiable under or over collection prior to the end of the reconciliation period for the objective of minimizing the impact of under or over collection by the reconciliation factor in the next year.
3. Cost of Purchased Gas – The estimated cost for gas purchased by the Company from its suppliers or the estimated weighted average prudently incurred cost for gas purchased by the Company from all sources where applicable. Such cost shall include not only the purchase cost of natural gas but shall also include all reasonable costs for services such as gathering, treating, processing, transportation, capacity and/or supply reservation, applicable line loss charges, storage, balancing including penalties, swing services, and any other related costs and expenses necessary for the movement of gas to the Company's city gate delivery points and customers. The Cost of Purchased Gas may also include costs related to the purchase and transportation of Renewable Natural Gas (RNG). Renewable Natural Gas is the term used to describe pipeline-quality biogas produced from various biomass sources through a biochemical process that has been processed to purity standards and is interchangeable with conventional natural gas. The Cost of Purchased Gas may also include the cost of carbon "Environmental Attributes" purchased and retired in association with the purchase of Renewable Natural Gas. Environmental Attributes means any and all credits, benefits, emissions reductions, offsets, and allowances, howsoever entitled, attributable to the production and delivery of Renewable Natural Gas, including but not limited to: (1) any avoided emissions of pollutants to the air, soil or water such as sulfur oxides (SOx), nitrogen oxides (NOx), carbon monoxide (CO) and other pollutants; (2) any avoided emissions of carbon dioxide (CO2), methane (CH4) and other greenhouse gases; (3) displacement or avoidance of any amount of conventional gas or fossil energy generation resources; and (4) the reporting rights to these avoided emissions. The Cost of Purchased Gas shall not include the cost of financial instruments unless the use of such financial instruments is approved in advance and in writing by the Director of the Oversight and Safety Division of the Railroad Commission of Texas. Such approval may be requested as part of the Company's annual gas purchase plan, which shall be submitted annually to the Commission no later than June 15.
4. Customer Rate Relief Component – The rate per billing unit charged in accordance with and specified on Rate Schedule CRR, the Customer Rate Relief Rate Schedule, if applicable, which is a non-bypassable charge as defined in Tex. Util. Code § 104.362(7).

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5. Reconciliation Component – The amount to be returned to or recovered from sales customers each month from December through August as a result of the Reconciliation Audit.
6. Reconciliation Audit – An annual review of the Company's books and records for each 12-month period ending with the production month of August to determine the amount of over or under collection occurring during such 12-month period. The audit shall determine: (a) the total prudently incurred amount paid for gas purchased by the Company (per Section B(3) above) to provide service to its sales customers during the period, including prudently incurred gains or losses on the approved use of natural gas financial instruments; (b) the revenues received from operation of the provisions of this Cost of Gas Clause reduced by the amount of revenue associated fees and taxes paid by the Company on those revenues; (c) the total amount of surcharges or refunds made to sales customers during the period and any other revenues or credits received by the Company as a result of relevant gas purchases or operation of this Cost of Gas Clause; (d) the total amount accrued for imbalances under the transportation rate schedule(s) net of fees and applicable taxes; (e) the total amount of Uncollectible Cost of Gas during the period; (f) the total amount of FERC Intervention Costs; and (g) an adjustment, if necessary, to remove lost and unaccounted for gas costs during the period for volumes in excess of 5 percent of purchases.
7. Purchase/Sales Ratio – A ratio determined by dividing the total sales volumes purchased for sales customers during the 12-month period ending June 30 by the sum of the sales volumes sold to sales customers. For the purpose of this computation all volumes shall be stated at 14.65 psia. Such ratio as determined shall in no event exceed 1.0526 i.e.  $1/(1 - 0.05)$  unless expressly authorized by the applicable Regulatory Authority.
8. Reconciliation Account – The account maintained by the Company to assure that over time it will neither over nor under collect revenues as a result of the operation of the Cost of Gas Clause. Entries shall be made monthly to reflect: (a) the total prudently incurred amounts paid to the Company's supplier(s) for gas applicable to sales customers as recorded on the Company's books and records (per Section B(3) above), including prudently incurred gains or losses on the use of approved natural gas financial instruments; (b) the revenues produced by the operation of this Cost of Gas Clause reduced by the amount of fees and taxes; (c) refunds, payments, or charges provided for herein or as approved by the Regulatory Authority; (d) amounts accrued pursuant to the treatment of imbalances under any transportation rate schedule(s); (e) the total amount of Uncollectible Cost of Gas during the period; (f) the total amount of FERC Intervention Costs; and (g) an adjustment, if necessary, for lost and unaccounted for gas during the period in excess of 5 percent of purchases.
9. FERC Intervention Costs – Costs prudently incurred from outside vendors and attorneys for the purpose of protecting the interest of sales customers in the West-North Service Area in connection with negotiating Federal Energy Regulatory Commission (“FERC”) related issues with upstream pipelines or intervention and participation in proceedings at the FERC. FERC Intervention Costs may also include prudently incurred internal travel expenses related to this purpose.
10. Uncollectible Cost of Gas – The amounts actually written off after the effective date of this rate schedule related to cost of gas will be tracked along with any subsequent recovery/credits related to the Cost of Gas Clause. Annually the charge offs minus recoveries will be included in the annual reconciliation and factored into the resulting Reconciliation Component.

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**C. COST OF GAS**

In addition to the cost of service as provided under its gas sales rate schedules, the Company shall bill each sales customer for the Cost of Gas incurred during the billing period. The Cost of Gas shall be clearly identified on each customer bill.

**D. DETERMINATION AND APPLICATION OF THE RECONCILIATION COMPONENT**

If the Reconciliation Audit reflects either an over recovery or under recovery of revenues, such amount, plus or minus the amount of interest calculated pursuant to Section E below, if any, shall be divided by the sales volumes, adjusted for the effects of weather, growth, and conservation for the period beginning with the December billing cycle through the August billing cycle preceding the filing of the Reconciliation Audit. The Reconciliation Component so determined to collect any revenue shortfall or to return any excess revenue shall be applied, subject to refund, for a 9 month period beginning with the December billing cycle and continuing through the next August billing cycle at which time it will terminate.

**E. INTEREST ON FUNDS**

Concurrently with the Reconciliation Audit, the Company shall determine the amount by which the Cost of Gas was over or under collected for each month, including any cost of gas inventory in storage and margins on non-utility transactions as described in paragraph "G" below, within the period of audit. The Company shall debit or credit to the Reconciliation Account for each month of the reconciliation period: (1) an amount equal to the outstanding over collected balance multiplied by interest of 6 percent per annum compounded monthly; or (2) an amount equal to the outstanding under collected balance multiplied by interest of 6 percent per annum compounded monthly. The Company shall also be allowed to recover a carrying charge calculated based on the arithmetic average of the beginning and ending balance of gas in storage inventory for the prior calendar month times the authorized rate of return.

**F. SURCHARGE OR REFUND PROCEDURES**

In the event that the rates and charges of the Company's suppliers are retroactively reduced and a refund of any previous payments is made to the Company, the Company shall make a similar refund to its sales customers. Similarly, the Company may surcharge its sales customers for retroactive payments made for gas previously delivered into the system. Any surcharge or refund amount will be included in the Reconciliation Account.

Refunds or charges shall be entered into the Reconciliation Account as they are collected from or returned to the customers. For the purpose of this Section F, the entry shall be made on the same basis used to determine the refund or charge component of the Cost of Gas and shall be subject to the calculation set forth in Section (E) Interest on Funds, above.

**COST OF GAS CLAUSE (Continued)**

**G. NON-UTILITY TRANSACTIONS**

The aggregate net margins generated by the company from all Non-Utility Transactions shall be divided between the Company and ratepayers with the Company retaining 33 1/3% of aggregate annual Net Margins generated from such activities and 66 2/3% shall be credited to sales customers in the month during which the transaction closes. For purposes of this provision, “Non-Utility Transactions” shall mean the following transactions to the extent that such transactions pertain to natural gas supplies, storage, and transportation capacity allocated to sales customers within the West-North Service Area: off-system sales of natural gas, releases of transportation or storage capacity, financial arbitrage of storage inventories, trading of natural gas inventories, and use of financial instruments pertaining to purchase, storage, and/or transportation of natural gas, so long as such instruments are not intended to hedge the cost of system supplies. “Non-utility Transactions” shall not include any transaction conducted by any affiliate of the company. For purposes of this provision, “Net Margins” shall mean revenues from the aggregate of all Non-Utility Transactions, less the costs to the Company of such transactions, including related taxes, commissions, transaction fees, and transfer fees. The Net Margins allocated to ratepayers shall be credited to the ratepayers once per year through an adjustment of the Reconciliation Account as determined in the Annual Reconciliation filing. The Company shall be fully responsible for any aggregate annual net losses incurred from such activities and no such losses shall be paid by the ratepayers. This provision does not permit the Company to include in the calculation of gas cost storage, or gas stored except as prudently and necessarily needed to serve sales customers in this service area.

**H. COST OF GAS STATEMENT**

The Company shall file a Cost of Gas Statement with the Regulatory Authority by the beginning of each billing month. The Cost of Gas Statement shall set forth: (a) the estimated Cost of Purchased Gas; (b) that cost multiplied by the Purchase/Sales Ratio; (c) the amount of the Cost of Gas caused by any surcharge or refund; (d) the Customer Rate Relief Component; (e) the Reconciliation Component; (f) the revenue associated fees and taxes to be applied to revenues generated by the Cost of Gas; (g) the Cost of Gas calculation, including gains and losses from approved hedging activities for the month; and (h) the beginning and ending date of the billing period. The statement shall include all data necessary for the Regulatory Authority to review and verify the calculations of the Cost of Gas.

**I. ANNUAL RECONCILIATION REPORT**

The Company shall file an Annual Reconciliation Report with the Regulatory Authority which shall include but not necessarily be limited to:

1. A tabulation of volumes of gas purchased and costs incurred listed by account or type of gas, supplier and source by month for the 12 months ending August 31.
2. A tabulation of gas units sold to sales customers and related Cost of Gas Clause revenues, excluding the Customer Rate Relief Component.
3. A tabulation of all other costs and refunds made during the year and their effect on the Cost of Gas Clause to date.

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4. A tabulation of any FERC Intervention activities performed and associated costs incurred on behalf of West-North Service Area sales customers.
5. A description of the hedging activities conducted each month during the 12 months ending August 31, including the types of transaction used, resulting gains and losses, any changes in the hedging program implemented during the period and the rationale for the changes. The report should include the customer impact of hedging activities stated as costs to the average residential and commercial customer during the period.
6. A description of the imbalance payments made to and received from the Company's transportation customers within the service area, including monthly imbalances incurred, the monthly balances resolved, and the amount of the cumulative imbalance. The description should reflect the system imbalance and imbalance amount for each supplier using the Company's distribution system during the reconciliation period.
7. A tabulation of Uncollectible Cost of Gas during the period and its effect on the Cost of Gas Clause to date.

This report shall be filed concurrently with the Cost of Gas Statement for December. If the Regulatory Authority thereafter determines that an adjustment to the Reconciliation Component is required, such adjustment shall be included in the Reconciliation Component for the next annual Reconciliation Audit following the date of such determination.