State of Florida

Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: November 20, 2007

TO: Office of Commission Clerk (Cole)

FROM: Division of Economic Regulation (Draper) EJD
Office of the General Counsel (Fleming) KEF S.M.C.

RE: Docket No. 070570-GP – Petition for approval of natural gas transmission pipeline tariff by Peninsula Pipeline Company, Inc.

AGENDA: 12/4/07 – Regular Agenda – Tariff Filing – Interested Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Administrative

CRITICAL DATES: April 27, 2008 – (8-Month Effective Date)

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\070570A.RCM.DOC

RECEIVED-FPSC
07 NOV 20 PM 3:59
COMMISSION CLERK

Case Background

On August 27, 2007, Peninsula Pipeline Company, Inc., (Peninsula), a subsidiary of Chesapeake Utilities Corporation, filed a petition for approval of an intrastate gas pipeline tariff. On September 2, 2005, Peninsula had filed a petition for a declaratory statement posing the question whether Peninsula, a corporation in its own right, is precluded from operating as a natural gas transmission company as defined in section 368.103(4), Florida Statutes (F.S.), by the fact that its parent corporation owns or operates facilities primarily for the local distribution of natural gas or that an affiliated corporation is subject to the jurisdiction of the Federal Energy Regulatory Commission (FERC) under the Natural Gas Act, 15 U.S.C. ss. 717 et seq. By Order

DOCUMENT NUMBER-DATE
10464 NOV 20 ♁
FPSC-COMMISSION CLERK

PSC-06-0023-DS-GP,[1] the Commission found that Peninsula, as a corporation with a separate legal identity from its parent corporation, qualified as a natural gas transmission company as defined in Section 368.103(4), F.S. In addition, the Commission stated it was important to distinguish between local distribution companies (LDCs) and transmission pipelines, "so that the captive ratepayers of Florida's LDCs and the competitive market for natural gas in Florida are not harmed by the transmission company's operations."[2]

Peninsula's proposed tariff would allow Peninsula to construct pipelines and engage in the business of transporting gas in Florida. At present, Peninsula has made no investment in pipeline facilities and serves no customers. Commission approval of the proposed natural gas transmission pipeline tariff would enable Peninsula to actively pursue transportation agreements with gas customers, and construct and operate intrastate pipeline facilities. The proposed tariff includes the general terms, conditions, and rules under which Peninsula proposes to operate. The tariff does not include rates and charges, as those would be negotiated individually with each customer pursuant to Section 368.105(3), F.S.

The Natural Gas Transmission Pipeline Intrastate Regulatory Act (the Act), Sections 368.101-368.112, F.S., was adopted by the Florida Legislature in 1992 in conjunction with Sections 403.9401-9425, F.S., the Natural Gas Transmission Pipeline Siting Act (Pipeline Siting Act). At the time they were enacted, these laws contemplated the filing of a proposal for a major gas pipeline (Sunshine Pipeline Partners) that would serve local distribution companies and major electric power generators in Florida and would be regulated by this Commission rather than the FERC.[3] The statute enables an intrastate pipeline company to be exempt from FERC jurisdiction under what is known as "the Hinshaw Amendment." The Hinshaw Amendment, contained in section 1(c) of the Natural Gas Act, 15 U.S.C. § 717(c), "exempts from FERC regulation intrastate pipelines that operate exclusively in one State and with rates and services regulated by the State." Payment of regulatory assessment fees to cover the cost of regulation and jurisdiction over pipeline safety is also provided for in Chapter 368, F.S.

The Pipeline Siting Act is administered by the Department of Environmental Protection (DEP). DEP is responsible for the certification of natural gas transmission pipelines, and the Commission is responsible for determining the need for intrastate gas transmission pipelines pursuant to Section 403.9422, F.S. Section 403.524, F.S., provides for certain exemptions. Pipelines that do not cross a county line, or are less than 15 miles in length do not need to be certified.

The Act and the Pipeline Siting Act have rarely been invoked since they were enacted 15 years ago. The major pipeline project was never constructed, and today there are no intrastate pipelines operating in the state. There is only one earlier instance of Commission approval of an

[1]Issued on January 9, 2006, in Docket No. 050584-GP, in Re: Petition for declaratory statement by Peninsula Pipeline Company, Inc. concerning recognition as a natural gas transmission company under Section 368.101, et seq.

[2] See Order No. PSC-06-0023-DS-GP, p. 4

[3] See Order No. PSC-93-0987-FOF-GP, issued July 2, 1993, in Docket No. 920807-GP, in Re: Application for a Determination of Need for an Intrastate Natural Gas Pipeline by Sunshine Pipeline Partners.

intrastate pipeline tariff.[4] Five Flags Pipeline Company provided natural gas transportation service to one customer, the Okaloosa County Gas District. Five Flags Pipeline Company notified the Commission of its dissolution on June 18, 1999.

For the reasons discussed below, staff is recommending that Peninsula's initial tariff, which would allow Peninsula to operate as a regulated intrastate gas pipeline, be approved.

The Commission has jurisdiction over this matter pursuant to Chapter 368, Florida Statutes.

[4] See Order No. PSC-97-0609-FOF-GP, issued on May 28, 1997, in Docket No. 970361-GP, in Re: Five Flags Pipeline Company – Petition for approval of existing firm and interruptible system transportation rates.

Discussion of Issues

Issue 1: Should the Commission approve Peninsula's proposed natural gas transmission pipeline tariff?

Recommendation: Yes, the proposed tariff should be approved pursuant to Chapter 368, F.S. Upon the issuance of the consummating order in this docket, Peninsula shall pay regulatory assessment fees as required by Rule 25-7.101, Florida Administrative Code (F.A.C.). Peninsula shall also file Annual Reports as required by Rule 25-7.100, F.A.C. Within 45 days after executing a transportation service agreement, Peninsula and the customer shall file an affidavit with the Commission as required by Section 368.105(3), F.S. Upon request by the Commission, Peninsula shall make available its negotiated Firm Transportation Service Agreements. (Draper)

Staff Analysis:

Background. Natural gas is delivered to Florida through four FERC regulated interstate transmission pipelines: Florida Gas Transmission Company (FGT), Gulfstream Natural Gas System, Southern Natural Gas, and Gulf South Pipeline. The gas entering Florida is delivered to new or re-powered electric generating facilities, large industrial customers, municipally-operated systems, and investor-owned LDCs. Pipeline laterals connect the transmission pipelines to the gas consumers listed.

Peninsula proposes to construct and maintain pipeline facilities that would transport gas from the interstate transmission pipeline, such as FGT, to new customers. Peninsula's proposed tariff refers to the customers of Peninsula's intrastate pipeline as "shippers." Peninsula will provide firm transportation service only and will not engage in the sale of gas. The new customer can be an industrial plant, an electric generation facility, a non-affiliated LDC, or a municipal system. A customer who chooses Peninsula to transport its gas is required to enter into a Firm Transportation Service Agreement with Peninsula.

The service provided by Peninsula is optional. Currently, pipeline laterals can be constructed by the customer itself, the interstate pipeline, or a LDC. Customers will continue to be able to choose their pipeline provider. Peninsula will simply be available as an additional transmission pipeline provider. In addition to building and maintaining the pipeline facilities, Peninsula will be responsible for providing administrative services related to the transportation of gas from the interconnection with the transmission pipeline to the point(s) of delivery (interconnection between Peninsula and customer).

Regulatory Authority. The Act provides for a different level of regulation than that afforded to LDCs or investor-owned electric utilities under Chapter 366, F.S. Section 368.105(3), F.S., allows rates charged by a natural gas transmission company to be deemed just and reasonable without explicit Commission approval if the rates meet certain conditions as listed below. Section 368.105(3), F.S., states:

> Rates charged or offered to be charged by any natural gas transmission company for transactions with other natural gas transmission companies, transportation customers, and industrial,

> power plant, and other similar large-volume contract customers, but excluding direct sales-for-resale to gas distribution utilities at city gates, unless suspended and modified pursuant to this subsection, are deemed to be just and reasonable and approved by the commission, if both the natural gas transmission company and the customer files an affidavit with the commission that:
>
> (a) Neither the natural gas transmission company nor the customer had an unfair advantage during the negotiations;
>
> (b) The rates are substantially the same as rates between the natural gas transmission company and two or more of those customers under the same or similar conditions of service; or
>
> (c) Competition does or did exist either with another natural gas transmission company, another supplier of natural gas, or with a supplier of an alternative form of energy.

Section 368.105(3), F.S., thus contemplates that gas transportation service provided by an intrastate pipeline is based on negotiated agreements that reflect market conditions and the specific needs of the customer. Peninsula will only provide transportation service and will not engage in the retail sale of natural gas. Title of the gas transported on Peninsula's facilities will belong to the customer. The customer is responsible for purchasing their own gas supplies. Section 368.105(6), F.S., further requires that rates not be unduly discriminatory and be cost compensatory. That section also requires the Commission to resolve any disputes between the natural gas transmission company and a person desiring transmission access.

Order No. PSC-06-0023-DS-GP set out certain parameters under which Peninsula would operate, in addition to the statutory requirements. These parameters were established primarily to ensure that Peninsula would not serve a customer within the existing service territory of a LDC, without first obtaining Commission approval, in order to protect the general body of LDC ratepayers. If a LDC looses a large customer to Peninsula, this could potentially shift costs to the LDC's remaining ratepayers. Peninsula's proposed tariff restates those parameters. Under its proposed tariff, Peninsula can provide service if the customer is currently not being served with natural gas by another entity and the location of the facilities to be served is greater than one mile in distance from existing gas facilities operated by an investor-owned gas utility, a gas municipality, or gas district. For example, if Peninsula wishes to serve an existing LDC customer, Peninsula will need prior Commission approval.

<u>Proposed tariff</u>. Peninsula's proposed tariff includes the rules and standard forms necessary to operate a natural gas transmission pipeline system. Peninsula states that the tariff provisions are standard practice in the gas industry. Such services include receipt and administration of scheduled gas quantities for the customer's account, resolution of monthly imbalances (difference between scheduled gas and gas used by customer), and other services. Peninsula will also operate as Delivery Point Operator (DPO). As DPO, Peninsula will be

responsible for ensuring that the gas being delivered by the interstate pipeline matches as closely as possible the amount of gas being consumed by the customer.

Market Opportunities. Peninsula asserts that it has opportunities to provide natural gas transmission service in certain markets throughout Florida. Peninsula further states that industrial customers are interested in customizing their gas transportation rates and service conditions to meet their specific operational and economic needs. The four interstate pipelines typically are only interested in the expansion of their system to large volume customers, such as electric generation facilities, that are willing to enter into long-term (20-year) contracts. Interstate pipelines do not find it economically feasible to expand or customize their services for an individual industrial customer.

An industrial customer currently has two choices to transport gas from the interstate pipeline to its facility: construction of a pipeline lateral or contracting with a LDC. Peninsula asserts that most industrial customers have little interest in investing capital in a pipeline, nor do they want to be responsible for the operation and maintenance of the facilities. A LDC that is considering extending the transmission pipeline system to reach a developing area is faced with the choice of building its own facilities, or contracting with another entity to build it. If the LDC builds its own facilities, the facilities become part of the LDC's investment in regulated rate base. However, LDCs may have capital constraints that limit their ability to construct facilities to reach newly developing areas. In addition, such projects may fail to meet the LDC's feasibility test. Pursuant to Rule 25-7.054, F.A.C, the maximum capital investment to be made by a LDC without cost to the customer is the maximum allowable construction cost, which is equal to four times the estimated annual gas revenue.

Peninsula will present an additional cost effective choice for customers who might otherwise not use natural gas. Individual contracts allow each end use customer to tailor the contract to specific needs. Since the customer has alternatives, the customer will negotiate a price that is acceptable for the benefits received on a market basis. When the LDC contracts with the interstate pipeline or Peninsula for capacity, the LDC may seek recovery of those transportation costs through the purchased gas adjustment (PGA). The Commission thus retains oversight over the rates charged by Peninsula to recover its investment to a LDC because these costs are subject to review as part of the LDC's PGA filing.

Conclusion. Peninsula's proposed tariffs are reasonable and meet the requirements of Chapter 368, F.S. Peninsula further states that it will comply with the Pipeline Siting Act when proposed pipelines fall within its requirements. Within 45 days after executing a transportation service agreement, Peninsula and the customer should file an affidavit with the Commission as required by Section 368.105(3), F.S. Upon the issuance of the consummating order in this docket, Peninsula should pay regulatory assessment fees as required by Rule 25-7.101, F.A.C. The Rule states that the regulatory assessment fee for natural gas transmission companies shall be 0.25 percent annually of the company's gross operating revenue. Peninsula should also file Annual Reports as required by Rule 25-7.100, F.A.C. Upon request by the Commission, Peninsula should make available its negotiated Firm Transportation Service Agreements. Staff envisions that obtaining copies of the agreements will only be necessary in the event of a customer complaint.

Issue 2: Should this docket be closed?

Recommendation: Yes. If Issue 1 is approved, this tariff should become effective on December 4, 2007. If a protest is filed within 21 days of the issuance of the order, this tariff should remain in effect, with any revenues held subject to refund, pending resolution of the protest. If no timely protest is filed, this docket should be closed upon the issuance of a consummating order. (Fleming)

Staff Analysis: If Issue 1 is approved, this tariff should become effective on December 4, 2007. If a protest is filed within 21 days of the issuance of the order, this tariff should remain in effect, with any revenues held subject to refund, pending resolution of the protest. If no timely protest is filed, this docket should be closed upon the issuance of a consummating order.