

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition of Florida  
Division of Chesapeake Utilities  
Corporation for authority to  
convert all remaining sales  
customers to transportation  
service and to exit merchant  
function.

DOCKET NO. 020277-GU  
ORDER NO. PSC-02-1646-TRF-GU  
ISSUED: November 25, 2002

The following Commissioners participated in the disposition of  
this matter:

LILA A. JABER, Chairman  
J. TERRY DEASON  
BRAULIO L. BAEZ  
MICHAEL A. PALECKI  
RUDOLPH "RUDY" BRADLEY

ORDER APPROVING PHASE I OF CHESAPEAKE UTILITIES CORPORATION'S  
PETITION TO CONVERT ALL REMAINING SALES CUSTOMERS TO  
TRANSPORTATION SERVICE AND TO EXIT THE MERCHANT FUNCTION

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service  
Commission that the action discussed herein is preliminary in  
nature and will become final unless a person whose interests are  
substantially affected files a petition for a formal proceeding,  
pursuant to Rule 25-22.029, Florida Administrative Code.

I. BACKGROUND

In April 2000, we adopted Rule 25-7.0335, Florida  
Administrative Code, which requires each local distribution company  
(LDC) to offer the transportation of natural gas to all non-  
residential customers. The rule further provides that each LDC may  
offer the transportation of natural gas to residential customers  
when it is cost effective to do so.

On March 28, 2002, Chesapeake Utilities Corporation filed its  
Petition for Authority to Convert All Remaining Sales Customers to  
Transportation Service and to Exit Merchant Function. In this

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Petition Chesapeake proposes to require all remaining sales customers to switch to transportation service.

The number of Chesapeake's non-residential sales customers has decreased substantially in the past few years due to restructuring of the gas industry. As these customers started buying gas on the open market, Chesapeake's transportation volumes increased and its sales volumes decreased. Prior to 2000, transportation service to non-residential customers comprised 70% of the Company's total system throughput, and it now comprises 96% of that throughput.

The remaining sales customers include 663 non-residential customers, all of whom are in the low usage rate classifications, and 9,587 residential customers. The non-residential customers account for 2.5% of the total system throughput and the residential customers account for 1.5% of the total system throughput. These customers require a small and seasonally variable volume of gas, factors that make the cost of the gas expensive.

Chesapeake believes gas marketers can sell gas to its remaining sales customers less expensively than Chesapeake can. Chesapeake has concluded that the only cost effective approach available to it is to completely exit the merchant function, and require all remaining sales customers to convert to transportation service. Chesapeake's Petition is for a new tariff which allows a gradual transition from sales service to transportation service for the remaining sales customers.

Customer meetings were held on June 25, 2002, in Winter Haven and St. Cloud, and on June 26, 2002, in Plant City and Crystal River.

Jurisdiction over this matter is vested in the Commission by several provisions of Chapter 366, Florida Statutes, including Sections 366.03, 366.04, 366.05, 366.06 and 366.075, Florida Statutes.

## II. PROVISIONS OF THE PROPOSED TARIFF

Under Chesapeake's proposal, a Transitional Transportation Service (TTS) tariff would be established to facilitate the conversion of remaining sales customers to aggregated customer

pools. Chesapeake would retain qualified gas marketers to administer the pools. These Pool Managers would have the capability of combining the gas supply requirements of customers in the TTS pools with other customers served by the Pool Manager, both on and off the Company's distribution system.

Chesapeake believes its customers' gas supply needs are best served by a gas marketer with the ability to "rebundle" the Company's small volume gas users into a diversified, state-wide customer group consisting of industrial and commercial customers with different levels of weather sensitivity and peak usage. The increased market power of a larger overall customer group, with greater gas volume requirements, would result in a higher probability of obtaining lower gas costs than would be achievable by the decreasing sales service volumes on the Company's system alone.

Chesapeake's approach will allow all stakeholders adequate time to develop the knowledge and experience needed for a successful transition to a fully competitive open market. Chesapeake would maintain a contractual relationship with the Pool Manager(s) throughout the transition period, which is designed to provide reliable service at reasonable prices, while gradually introducing more options and choices to a better informed customer group.

The TTS tariff includes a phased in transition period to be completed over several years. In addition, to avoid any conflict of interest or appearance of impropriety, the Company will exclude its own marketing affiliate from participating in all phases.

The implementation of Phase One would be for a two-year period where all remaining residential and non-residential sales customers would receive gas supply service through one qualified Pool Manager, selected by the Company through a Request for Proposals (RFP) process. The TTS agreement between the Company and the selected Pool Manager would be structured to provide customers the opportunity to select between two pricing options: a monthly indexed price, similar to the current PGA pricing mechanism, or a fixed price option that enables customers to mitigate the potential price volatility of the monthly indexed price.

Near the end of the initial two-year period, the Company would evaluate customer acceptance of the program, assess its own capabilities to expand program options, and make a determination of the feasibility and timing for initiating Phase Two. Chesapeake would also report to the Commission on the results of Phase One, and the customer education and implementation plan for Phase Two. After submitting the report, Chesapeake would petition for approval to start implementing Phase Two.

Phase Two would expand the choices available. The Company would retain, through an RFP process similar to that used in Phase One, a minimum of two Pool Managers. The Company would require each Pool Manager to offer a range of gas pricing terms and conditions. Customers would have the ability to choose between the two Pool Managers, and select the pricing option that best matched their individual circumstances. At the end of Phase Two, the Company would report to us on the results of Phase Two, and the Phase Three customer education and implementation plan. The duration of Phase Two is left open, but is expected to be at least one year.

Phase Three would completely transition customers to a fully competitive marketplace. With its customers being better informed and having several years of experience with gas marketers and various pricing options, the Company would replace the TTS tariff with its Aggregated Transportation Service Program. Customers would be free to choose any Pool Manager authorized to deliver gas on the Company's distribution system, and negotiate price and other terms with no constraints imposed by the Company. Pool Managers would be authorized to directly solicit any and all customers for gas supply services.

The Company's proposal is carefully designed to avoid exposure of its customers to the risk of service disruption. The TTS Agreement provides for severe financial penalties and potential termination of the agreement in the event that the TTS Pool Manager fails to deliver gas. The Company is prepared to act as the supplier of last resort in the case of longer term problems.

The TTS Agreement would specifically define the Pool Managers' actions or omissions constituting a default, including: failure to observe the terms and conditions of the TTS Agreement; failure in

performance of essential duties and obligations such as failing to deliver gas for an extended period without prior approval, force majeure, or re-relinquishing capacity outside the contract limits; engaging in price gouging, slamming or other improper or unlawful activities; and, failure to maintain financial viability.

Chesapeake would implement procedures and provide the oversight necessary to ensure continuity of service to the pool customers in a default situation. If the Pool Manager defaults during Phase One, the Company would act to terminate the TTS Pool Manager and, as the supplier of last resort, would recall the interstate pipeline capacity, arrange for gas supply, and perform all other necessary functions to ensure delivery to affected customers. If during Phase Two, either of the two TTS Pool Managers defaults, the non-defaulting Pool Manager would assume gas delivery responsibilities for all customers until arrangements to qualify a replacement Pool Manager could be made. If both Pool Managers default, the Company would act as the supplier of last resort, would recall the interstate pipeline capacity, arrange for gas supply, and perform all other necessary functions to ensure delivery to affected customers, until arrangements to qualify replacement Pool Managers could be made.

For the residential and small commercial customers transitioning from sales to transportation service, the Company would maintain the customer service function, maintain customer account transaction records, and provide gas supply billing and collections indefinitely. Customers would continue to receive one monthly bill, and the Pool Managers' charges would appear in lieu of the Company's purchased gas adjustment. The Company would follow a prescribed hierarchy in applying customer payments. All payments would first be applied to any taxes and fees imposed by government; second, to Pool Managers' charges for gas supply; and third, to the Company's regulated transportation charges. Customers currently taking service under the transportation tariff (primarily large commercial and industrial customers) would have the option of getting billed directly from the marketer serving them or through Chesapeake.

This payment hierarchy would enable the Company to retain the capability to disconnect customers for non-payment in the event of a partial payment. Applying the payment to the Pool Manager's gas

supply cost prior to the Company's regulated charges would prevent customers from taking advantage of the absence of the Pool Manager's service disconnect authority by paying only the regulated charges. However, this arrangement would not provide protection to the Pool Manager in the event that the customer failed to pay at all. The Pool Manager would have the authority to appropriately secure customer accounts through cash deposits or similar means.

Chesapeake currently has the authority to collect a charge from Pool Managers opting to receive customer billing and payment processing services from the Company, in the amount of \$5.00 per bill, applicable to the limited number of non-residential customers receiving transportation service. The Company proposes to reduce this charge to \$2.00 per account per month applicable to all accounts receiving service from Pool Managers. The charge would be mandatory for the TTS Pool Managers, but remain elective for Pool Managers and other gas marketers serving non-residential accounts in the Company's aggregated or individual transportation service programs. The revenue generated by this charge will go to offset the costs needed to implement the computer systems necessary to accommodate a total customer transportation service environment.

As the Company prepares to exit the merchant function, participation in the purchased gas cost recovery proceedings will no longer be necessary. The Company filed its final true-up for the calendar year 2001 in the PGA docket in May 2002, indicating an over-recovery. Projected filings are due in September 2002, to determine the PGA cap for the year 2003. However, upon the activation of service by the Phase One TTS Pool Manager, there would cease to be any need for the Company to have an active PGA mechanism. We will review whatever over or under-recovery may have accrued at that time for appropriate disposition by the Company. Chesapeake proposes to address that matter in a subsequent filing within ninety days of the termination of its gas sales merchant function. Based on the most recent data, it appears that the company will be in an over-recovery state for the period ended August 31, 2002.

The Company has submitted revised tariff sheets that incorporate the changes necessary to implement transportation service to all remaining sales customers.

### III. ANALYSIS

Chesapeake cites Rule 25-7.0335, Florida Administrative Code, as authority for approving the Petition. The rule requires that each local distribution company (LDC) "offer" the transportation of natural gas to all non-residential customers. The rule further provides that each LDC "may offer" the transportation of natural gas to residential customers when it is cost effective to do so.

Chesapeake's request in the Petition falls outside the scope of the rule. The rule requires that LDC's "offer" transportation service to non-residential customers and that LDC's "may offer" such service to residential customers. The rule does not allow LDC's to require that any customer switch to transportation service. Chesapeake's proposed TTS tariff requires customers to switch from sales to transportation service and so the rule is inapplicable.

Under Section 366.075, Florida Statutes, we have the authority to approve experimental and transitional rates. This section provides sufficient authority for the action we take herein.

Because Chesapeake's proposal presents us with a case of first impression, and is a step toward restructuring of the gas industry in Florida, we wish to proceed with caution. Based on the Company's Petition, we find that Phase I of Chesapeake's proposal to convert all remaining sales customers to transportation service and to exit the merchant function is appropriate and reasonable, and is hereby approved as an experimental and transitional pilot program pursuant to Section 366.075, Florida Statutes. In addition to the two-year report contemplated in the Company's Petition, Chesapeake shall provide a similar interim report to this Commission regarding Phase One. The report shall be submitted no later than 90 days from the conclusion of the first twelve months of the implementation of Phase I. The tariff shall become effective on November 5, 2002, and the interim report is due no later than 90 days after November 5, 2003. Further, all of the revenues and costs associated with the implementation of Phase One shall be accounted for above the line.

We believe it is reasonable and prudent to monitor the results of the implementation of Phase One before ruling on the Company's

request regarding Phases II and III. Therefore, we will not address nor make a determination as to Phases II and III at this time. Any change to Phase I, either to terminate its implementation or to proceed to Phases II or III, shall require an affirmative act of this Commission.

If a protest is filed within 21 days of this Order approving Chesapeake's tariff by a person whose substantial interests are affected, the tariff shall remain in effect pending resolution of the protest, with any charges held subject to refund pending resolution of the protest. If no protest is filed, this docket shall be closed upon the issuance of a Consummating Order.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that Phase I of Chesapeake Utilities Corporation's Petition for Authority to Convert All Remaining Sales Customers to Transportation Service and to Exit Merchant Function is approved as an experimental and transitional pilot program pursuant to Section 366.075, Florida Statutes. It is further

ORDERED that in addition to the two-year report contemplated in the Company's Petition, Chesapeake shall provide a similar interim report to this Commission regarding Phase I. The report shall be submitted no later than 90 days from the conclusion of the first twelve months of the implementation of Phase I. It is further

ORDERED that the tariff shall become effective on November 5, 2002. It is further

ORDERED that all of the revenues and costs associated with implementation of Phase I shall be accounted for above the line. It is further

ORDERED that any change to Phase I, either to terminate its implementation or to proceed to Phases II or III, shall require an affirmative act of this Commission. It is further

ORDERED that if a protest is filed within 21 days of this Order approving the tariff by a person whose substantial interests

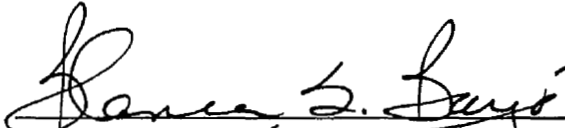


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are affected, the tariff shall remain in effect pending resolution of the protest, with any charges held subject to refund pending resolution of the protest. It is further

ORDERED that if no protest is filed, this docket shall be closed upon the issuance of a Consummating Order.

By ORDER of the Florida Public Service Commission this 25th day of November, 2002.

  
BLANCA S. BAYÓ, Director  
Division of the Commission Clerk  
and Administrative Services

( S E A L )

MKS

CONCURRENCE

Commissioner Palecki concurs in the decision.

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NOTICE OF FURTHER PROCEEDINGS

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

The Commission's decision on this tariff is interim in nature and will become final, unless a person whose substantial interests are affected by the proposed action files a petition for a formal proceeding, in the form provided by Rule 28-106.201, Florida Administrative Code. This petition must be received by the Director, Division of the Commission Clerk and Administrative Services, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on December 16, 2002.

In the absence of such a petition, this Order shall become final and effective upon the issuance of a Consummating Order.

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.