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February 2, 2005

VIA HAND DELIVERY

Division of Records and Reporting  
Florida Public Service Commission  
2540 Shumard Oak Boulevard  
Tallahassee, Florida 32399-0850

RE: Florida Division of Chesapeake Utilities Corporation

To the Clerk:

Pursuant to Order No. PSC-02-1646-TRF-GU, enclosed herewith on behalf of the Florida Division of Chesapeake Utilities Corporation is a Report on "Year Two" of the Company's Transitional Transportation Service Experimental Pilot Program. Please stamp and return one copy to my office acknowledging receipt.

Sincerely,  
ROSE, SUNDBSTROM & BENTLEY LLP

*Wayne L. Schiefelbein*

Wayne L. Schiefelbein  
Of Counsel

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Chesapeake Utilities Corporation, Florida Division  
Transitional Transportation Service Experimental Pilot Program  
Report to the Florida Public Service Commission  
Year Two of Implementation  
Order No. PSC-02-1646-TRF-GU

February 2005

**TTS Program Approval**

The Florida Public Service Commission (the Commission) in Rule 25-7.0335, F.A.C., (approved April 4, 2000) required each local distribution company (LDC) to offer gas transportation service to all non-residential customers. The Rule also offered LDCs the option to provide transportation service to residential customers. By Order No. PSC-02-1646-TRF-GU issued on November 25, 2002, the Commission approved a petition filed by the Florida Division of Chesapeake Utilities Corporation (Company) to transfer all of its remaining sales customers to a Transitional Transportation Service (TTS) program and exit the natural gas merchant function.

The Company's petition included a multi-phased program that, over several years, would transition all customers to a competitive marketplace with multiple gas suppliers. The Commission authorized the Company to implement the first phase of the TTS Program on an experimental, pilot basis. The Commission ordered that all expenses and revenues related to the program be accounted for above the line, in a "business as usual" manner. All costs and revenues related to the program would be subject to typical earnings surveillance and rate of return authorizations. The Commission also ordered that the Company, in a subsequent filing, address the appropriate disposition of any over or under-recovery in its Purchase Gas Account (PGA) following the exit of the merchant function.

The Commission Order required the Company to file a report on the results of the program within 90 days of the end of each of the first two years of implementation. The Company's report on the first year of implementation was filed in February 2004. This report provides an overview of the TTS Program following its second year of operation.

**Year One Implementation Overview**

The Company implemented Phase One of the approved TTS Program in November 2002, and assigned 9,587 residential and 552 non-transporting small commercial customers to Infinite Energy, the gas marketer selected by competitive bid to manage the TTS customer pool during the first phase of implementation. During the program's first year (2003) the Company

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implemented its approved program design and worked to complete its transition out of the merchant function.

- A TTS Pool Manager (gas marketer) was selected by competitive bid to provide gas supply and pipeline capacity management services to TTS customers. The contract term was for an initial two-year period with an option to renew the agreement for an additional year.
- Two open enrollment periods were provided during which 217 non-residential customers elected to select their own gas marketer and exit the TTS Pool.
- All of the Company's interstate pipeline capacity was allocated to the various shippers on its distribution system, including the TTS Pool Manager, based on a methodology approved by the Commission.
- The Company established procedures to ensure that it could act as the Supplier of Last Resort in the event the Pool Manager was unable to reliably deliver gas.
- The Company implemented a Customer Account Administrative Service (CAAS) that provides customer billing, collection services, payment tracking, non-pay disconnects and related administrative services to the Pool Manager. The Company provides such a service to simplify the transportation process for customers, to virtually eliminate the potential for "slamming," and to ensure that the fuel rates billed to TTS customers are appropriate.
- The Company implemented a prescribed hierarchy in applying TTS customer payments. All payments are first applied to any taxes and fees imposed by government; second, to Pool Managers' fuel charges for gas supply; and third, to the Company's regulated transportation charges. This payment hierarchy enables the Company to retain the capability to disconnect customers for non-payment or partial payment and appropriately protect the TTS Pool Manager from customers attempting to "game the system" by attempting to only pay the regulated charges.
- Several upgrades to the Company's Customer Information System (CIS) and internal administrative systems were implemented to support the TTS Program.
- The Company discontinued all gas commodity purchases and retail fuel sales upon implementation of the program.
- The Company discontinued its PGA account at the end of August 2003 and activated its approved Operational Balancing Account on September

1, 2003. On September 30, 2003 the Company filed a petition with the Commission for the final disposition of the PGA. The Commission staff conducted a PGA true-up audit during the month of October 2003 for the audit period November 2002 through September 2003. The staff audit concluded that the final PGA balance was \$246,255 over-recovered.

- The Company worked with Commission staff to evaluate both current and projected savings for all TTS pool customers. Based on the analysis, the Company petitioned the Commission for authority to restructure its smallest volume rate class (0 to 500 annual therms) into three new rate classes, with lower Customer Charges for the two smallest volume classes. The new rates and classifications went into effect on July 15, 2003.
- The Company's TTS Pool Manager offered customers two opportunities during 2003 to establish a fixed monthly fuel price over an annual period as an alternative to a fluctuating monthly index fuel price. In total, 1628 customers, representing over 15% of the TTS customer pool elected the fixed price option.

### **Year-Two Program Status**

As noted above, during the program's first year the Company worked to complete several actions required to transition out of the gas supply merchant function. By the midpoint of the second year of implementation, these transitional actions were complete. The Company's remaining PGA balance had been refunded to customers. The Operational Balancing Account was allocating transportation related imbalance charges and credits and pipeline operational control charges to shippers on the Company's distribution system. All new residential customers, and those commercial accounts not selecting their own marketer, were assigned to the TTS Pool using procedures generally transparent to the customers. Interstate pipeline capacity was re-assigned among Pool Managers as non-residential customers opted out of the TTS Pool, or as they moved from one pool to another. The CAAS service provided by the Company to the TTS Pool Manager routinely handled customer accounts with virtually no negative customer feedback. At this point, the TTS Program has effectively integrated residential and small commercial customers into the Company's normal operating practice for transportation service.

An overview of the current TTS Program status and the primary activities undertaken in 2004 is summarized below:

- At December 31, 2004, the TTS Program was serving 11,310 residential and 424 non-residential customers (11,734 total customers).

- Customers continue to realize overall gas cost savings through a reduction in various state and local taxes that do not apply to gas transportation service.
- A significant cost savings for TTS customers was achieved through the Company's efforts to reallocate and relinquish quantities of interstate pipeline capacity that were held for peaking and growth purposes. Historically, the cost of these capacity quantities was recovered from sales customers through the Company's PGA mechanism. As a result of the capacity reallocation and relinquishment efforts, the amount of capacity being allocated to the TTS Pool is substantially less than what was recovered through the PGA. The TTS Pool Manager is contractually obligated to deliver quantities sufficient to meet the daily requirements of the customer pool. Given the dynamic capacity market in Florida, especially during the TTS Pool's winter season peak usage period, meeting an occasional peak day does not cause problems for the TTS Pool Manager. There is no need to hold capacity at peak day quantities for occasional use during the winter. In its first report to the Commission the Company calculated annual capacity costs to the TTS Pool have been reduced by approximately \$849,000. Cost savings related to interstate pipeline capacity continued during 2004.
- The final action required to completely transition out of the merchant function was the disposition of the Company's remaining PGA balance. Based on the PGA true-up audit conducted by Commission staff in October 2003, the Commission issued Order No. PSC-04-0083-PAA-GU, on January 26, 2004, authorizing the Company to refund \$246,255 to all customers who received sales service in 2002. The Company completed the customer refunds during the billing month of March 2004. Based on the approved Commission refund methodology, the average residential customer received a refund in the amount of \$22.50.
- A central feature of the Company's TTS Program was the Customer Account Administrative Service (CAAS) This service would include billing, collection services, payment tracking, non-pay disconnects, various account reports and related administrative activities. The Company proposed such a service to simplify the transition for customers, to virtually eliminate the potential for "slamming," and to ensure that the fuel rates billed to TTS customers are in compliance with the Pool Manager Agreement. During 2004 the Company worked closely with Infinite Energy to improve in the following areas: the transmittal of reports, account usage data, capacity re-allocations, notice of customer additions and deletions, bad debt records and non-payment disconnect notices. Several modifications to the Company's CIS and other internal systems were implemented. At this point, the CAAS is fully operational. Both the

Company and TTS Pool Manager are satisfied with the level of service provided through the CAAS.

- The TTS Program's payment hierarchy procedure approved by the Commission is working as designed. The procedure has virtually eliminated attempts by customers to submit partial payment for only the regulated transportation charges and avoid service disconnections.
- During the first year of program operation, two open enrollment periods (January and September 2003) were offered to allow non-residential customers the opportunity to transfer out of the TTS Pool and into one of the Transportation Aggregation Service (TAS) pools operated on the Company's distribution system. A notice was provided to customers and the TTS and TAS Pool Managers. One of the few customer concerns the Company received about the TTS Program was the inability of a non-residential customer to opt out of the TTS Pool. On several occasions non-residential new construction customers failed to select a TAS Pool Manager prior to service initiation. These customers were automatically assigned to the TTS Pool and could not exit the pool until the next open enrollment period.

In 2004, the Company determined that its internal administrative capabilities were sufficient to allow a permanent open enrollment period. At any time during the year non-residential customers could notify the Company they were opting out of the TTS Pool and choosing their own gas marketer. These customers would be subject to the Company's general tariff rules for switching Pool Managers (thirty day notice; effective on the first day of the month following the notice period). This procedural adjustment provides non-residential TTS Pool customers the same opportunity to choose a gas marketer as is afforded the Company's other non-residential customers. The permanent open enrollment notice to customers and Pool Managers was mailed in October 2004.

- The Company conducted an audit of the TTS Pool Manager during 2004. The initial site visits occurred in January 2004. Additional examination of the Pool Managers records was undertaken to assure that customer billing was appropriate and in accordance with the TTS Agreement. The Company found the TTS Pool Manager to be substantially in compliance with the TTS Agreement. The Company and Pool Manager jointly identified several administrative and record-keeping issues that could be improved. As noted above, the Company has worked with the Pool Manager to improve information exchange and account administration.
- The Company retained the services of an outside consultant to conduct a series of focus groups with customers during 2004. Mel Juado, Ph.D., of the Profitable Group in Tampa, Florida facilitated the focus group

discussions. The focus groups were designed to cover a wide range of topics on customer service and various programs offered by the Company. The overall intent was to assess customer satisfaction and begin to develop benchmarks to measure future performance. The focus groups were not specifically targeted to review the TTS Program. However, the facilitator inquired about the program and received several comments from group participants. The consultant report noted that, "Forum participants across the board expressed satisfaction with CFG negotiating rates for them (through the RFP selection process to retain a TTS Pool Manager) and having the opportunity to lock rates in". The Company's customer service representatives report virtually no negative comments from customers on the TTS Program in 2004. When comments have been received they are almost exclusively related to the opportunity to participate in the next fixed price offer from the Pool Manager. Customers appear to have accepted the program as the operating norm on the Company's distribution system.

- At the end of 2003, the TTS Pool Manager, in conjunction with the Company, offered TTS customers the option to establish a fixed gas price for a twelve-month period. During two enrollment periods 1628 customers (15% of total customers at that time) signed up for the fixed price. The TTS Pool Manager originally intended to offer a new annual period fixed price in the fall of 2004. However, market pricing for natural gas in the last quarter of 2004 reached near record levels, helped in part by the hurricane activity in the Gulf of Mexico. Both the Company and TTS Pool Manager determined that the best interests of the TTS customers would be served by delaying any new fixed price offer until futures pricing returned to more stable levels. The January 2005 NYMEX price was \$1.73 per Dt lower than the December 2004 price. The twelve-month NYMEX gas futures price has also experienced a significant drop.

The Company's agreement with the current TTS Pool Manager expires in November 2005. The TTS Pool Manager is prepared to offer a new fixed price for a six-month period through the expiration of their agreement. The Company plans to issue an RFP for the selection of a new TTS Pool Manager by the end of August 2005. A fixed price offer that covers the 2005-2006 winter season could be offered to customers in September 2005 for an effective period beginning in November 2005, coinciding with the effective date of the new TTS Pool Manager.

- During the November 5, 2002, Agenda Conference the Commission requested that the Company provide the Florida legislature an opportunity to review and comment on its TTS Program and overall unbundling activities. To date, the legislature on at least two occasions had an opportunity to review the Company's program. The Florida Senate Committee on Finance and Taxation published Report Number 2003-124

in January 2003 entitled, "Implications of the Absence of a Use Tax on Utilities for Education Funding". This report included a detailed description of deregulation activities in the utility industry including recent actions by Florida gas distributors. The Senate report specifically referenced (pages 7 and 8) the Commission's approval of both the Chesapeake Utilities and Indiantown Gas Company unbundling programs.

The Company also presented a copy of its first year report to the Commission on the TTS Program (February 2004) to the Senate Utilities and Telecommunications Committee and the House Business Regulation and Consumer Affairs Committee. The staff directors of both committees received the report and a personal briefing on the program. In addition, the Company plans to submit a copy of the second year report to the appropriate Senate and House committees later this month. To date, the Company has received no negative comments on their program from the legislature.

### **Future Activities**

During the TTS Program's first two years the Company completed its transition out of the merchant function and put into practice the procedures required to administer a transportation-only distribution system. While the Company will continue to work on future enhancements to its systems and procedures, the TTS Program is fully operational. Customer satisfaction with the program is high. The Company's contractual relationship with the TTS Pool Manager has resulted in reliable, cost competitive gas supply service to small volume customers. At this point, the program has become part of the Company's routine business activity.

The Company believes that it is appropriate to convert the TTS Program from an experimental, pilot program to a permanent feature of its tariff. The Commission Order authorizing the program indicated that no substantive change to the program could occur without an affirmative action by the Commission. The Company intends to petition the Commission during 2005 to terminate the experimental status of the program, and permanently convert all of the Company's customers to transportation service.