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October 10, 2005

Blanca S. Bayo, Director
Commission Clerk & Administrative Services
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

RE: Peninsula Pipeline Company, Inc. (PPC)
Docket No.: 050584-GP

Dear Ms. Bayo:

CMP ____
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OTH ____

Enclosed herewith on behalf of Peninsula Pipeline Company, Inc. (PPC) for filing in the above docket, are an original and fifteen copies of PPC's Response to Questions from the Florida Public Service Commission (FPSC) Staff.

Please stamp and return a copy to my office acknowledging receipt.

Sincerely

Wayne L. Schiefelbein

Wayne L. Schiefelbein
Of Counsel

WLS/dcr
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Peninsula Pipeline Company, Inc. (PPC)
Petition for Declaratory Statement
Docket No. 050584-GP
Response to Questions
From
The Florida Public Service Commission (FPSC) Staff

Peninsula Pipeline Company appreciates the opportunity to respond to FPSC Staff questions regarding our petition for a declaratory statement. As we noted therein, the principal objective of our petition is to receive a determination from the FPSC on the recognition of PPC as an intrastate pipeline company under Section 368.101, Florida Statutes, et seq. In the absence of such recognition to date, PPC has not invested the resources to engage potential customers in substantive discussions of potential intrastate pipeline projects. In working to develop a general business model, several conceptual projects have been identified. Virtually no engineering or financial feasibility work has been conducted. Several of staff's questions are seeking technical information that can only be obtained when specific projects are identified. Other questions involve rate and service issues that PPC would expect to address during the FPSC's consideration of a subsequent tariff filing. In the event PPC receives a favorable determination on its petition, we look forward to working with the FPSC and its Staff to design the appropriate policies, terms and conditions of service and rate structure for a regulated intrastate transmission company.

<u>FPSC Staff Question No. 1:</u> On page 12 of your petition, you indicate that there are three types of projects that are contemplated for Peninsula Pipeline Company. Please provide the following information for each project type:

a. What would be a typical length and size of pipe for each of these types of projects?

   <u>PPC Response:</u> As noted above, PPC has not yet conducted an engineering study of any specific projects. However, given the location of existing and proposed interstate pipeline routes PPC would presume that the majority of projects would be less than fifteen miles in length and remain inside one county. Projects that exceed these limits would, as we understand the NGPSA, would require a need determination from the FPSC and permitting through FDEP. At this point, the cost of permitting a transmission pipeline under the NGPSA would preclude most small-scale projects. As noted in the petition, PPC would primarily seek to serve large-volume industrial or electric generating loads and support expansion or system improvement for LDCs. Pipe sizes would likely range from 4 inch up to 16 inch. There are potential projects that could involve pipeline construction through multiple counties with pipe sizes above 20 inches. PPC looks forward to working with the FPSC and its Staff on the need determination and permitting if such an opportunity materializes.

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b. What would be the typical operating hoop stress for each of these types of projects?

PPC Response: At this time, PPC has not determined a "typical" operating hoop stress for any project.

c. Will any of these projects operate at a hoop stress less than 20 percent?

PPC Response: PPC could envision operating certain projects at a hoop stress less than 20 percent of SMYS, if such operating conditions are allowed by state statute or FPSC rule.

FPSC Staff Question No. 2: Would Chesapeake Florida Division be capable of providing service to any of the three types of projects identified on page 12? If the response is in the negative, please explain why Peninsula Pipeline would be capable of providing service and Chesapeake Florida Division would not.

PPC Response: Any Local Distribution Company (LDC) regulated by the FPSC could provide service to the three types of projects identified on page 12 of the PPC petition, either through existing tariff provisions or by seeking FPSC approval of a Special Contract. Municipal gas systems or Special Gas Districts could also pursue such projects with the approval of their respective Commission or Board.

FPSC Staff Question No. 3: With respect to project type "c", would the interconnecting line between the LDCs be of the same pressure, higher, or lower?

PPC Response: PPC would design, construct and operate facilities interconnecting local distribution systems to ensure safe, reliable service under the operating conditions dictated by the specific project. At this time, no such specific projects of this type are under consideration. In the absence of the specifications under which a given project would operate, it is not possible to comment on pressure requirements. PPC can envision projects that would operate under each of the pressure conditions identified on page 12 of its petition.

FPSC Staff Question No. 4: In your petition beginning on page 13, you state that there are four primary factors that affect the feasibility and practicality of a small volume customer committing to a direct interstate pipeline connection.

a. Would Peninsula Pipeline charge a potential customer the cost of a tap, gate station, and/or related interconnection facilities? If not, why?

PPC Response: PPC would design its service agreement with a customer to recover the reasonable cost of all facilities provided to serve the customer either through a direct charge, as part of the rate for service, or through a surcharge or other mechanism, if such mechanism were approved by the FPSC.

b. Would a potential customer of Peninsula Pipeline be required to commit to a long-term agreement?

   PPC Response: The conditions under which service is provided to any customer, including the term of the agreement, would be subject to negotiation. The negotiation would consider the project's investment cost, risks and potential return as factors in determining the term of the service agreement.

c. Would Peninsula Pipeline negotiate "off-tariff" rates and services and/or a special contract for every customer?

   PPC Response: As required by Sec. 368.105(1), F.S., the rates and services provided by PPC would be consistent with schedules, rules and regulations on file with the FPSC. If the FPSC recognizes PPC as a natural gas transmission company under Section 368.101, F. S., PPC intends to seek approval of an intrastate pipeline transmission tariff. The PPC tariff would generally follow the format of FERC pipeline and FPSC distribution system tariffs. The standard terms and conditions of service would be defined by the PPC tariff. PPC envisions that, under the terms of the tariff, a service agreement would be executed with each customer.

   Sec. 368.105(3) F.S., provides for certain conditions under which rates between PPC and, "gas transmission companies, transportation customers, and industrial, power plant, and other similar large-volume contract customers, may be negotiated." Please see paragraphs 11-16 in the PPC petition. As noted in the PPC petition, large-volume customers are sophisticated procurers of energy and often approach gas service negotiations with the full intention of customizing the rates and service conditions to meet their specific operational or economic situation. There are several variables that enter into any rate discussion with a potential large- volume customer. PPC addressed several of these issues in its petition: a) the ability or interest of the customer to provide capital, b) competing fuel costs, c) the customer's creditworthiness, d) the customer's access to interstate pipeline capacity, e) term of the agreement, f) seasonal or other operating conditions, etc.

   It is rare that an LDC seeking to provide service to a large-volume customer would offer the customer a tariff rate. Virtually all large-volume LDC accounts added to a distribution system over the past five years are served through a negotiated Special Contract or other "off-tariff" mechanism. PPC intends to recover the cost to provide service and produce a return on investment from each customer through rates and service conditions that are competitive with a customer's alternatives. In most cases, achieving that objective would require a negotiated rate.

Further, consistent with the spirit of the NGTPIRA, in the event that PPC provides service to an affiliate or an LDC on a sale for resale basis, PPC would provide such service at FPSC-approved recourse rates. Such rates would be incorporated in the PPC tariff.

<u>FPSC Staff Question No. 5:</u> In your petition on page 25 you discuss several levels of risk.

a. Explain how Peninsula Pipeline, operating under NGTPIRA, NGPSA, and Commission rules would be better able to structure creative and flexible agreements to address and or mediate levels of risk.

   <u>PPC Response:</u> There are two principal risks that PPC believes can be addressed through authorization of its intrastate pipeline. First, there is the risk that potential large-volume customers will select an alternate fuel because the interstate pipelines are unwilling to alter their tariff rates, service provisions, cost recovery requirements and/or the length of their contract term. As noted in its petition, for those large-volume customers with negotiated agreements PPC would be able to customize rates and service terms to accommodate the customer's needs, assuming a reasonable return is also obtained. A local distribution system could also structure such an agreement with similar levels of creativity and flexibility. However, the second principal risk occurs when a customer reduces or terminates service and strands the investment cost that was required to extend service. In most instances where an LDC is providing service any stranded investment is ultimately recovered from the general body of ratepayers through rate adjustments, subject to FPSC approval. Under the proposed "Parameters of Service" included in paragraph 45 of its petition, PPC would bear all the risks of the capital investment for a negotiated rate customer in the event of customer defaults, plant closures or other similar events. PPC believes that the NGTPIRA offers an opportunity to craft creative agreements that include appropriate risk/reward provisions for the intrastate pipeline, without putting LDC ratepayers at risk.

b. If Peninsula Pipeline made a significant capital investment to serve a small industrial customer, would the pipeline be at risk if the customer reduced his service or terminated service?

   <u>PPC Response:</u> Based on PPC's understanding of the NGTPIRA, the recovery of stranded capital investment costs from other pipeline customers is not specifically addressed. The NGTPIRA provides the FPSC with significant regulatory oversight of intrastate pipelines, especially related to the establishment of just, equitable and sufficient rates. The recovery of stranded investments from other pipeline customers is a topic best handled by the FPSC during a rate proceeding. However, as a general rule, PPC would have no objection to assigning the investment risk to the transmission company for

industrial customers with negotiated rates. As noted above, PPC's proposed "Parameters of Service" would shift all the risks of the capital investment for a negotiated rate customer to PPC. The opportunity to negotiate rates with individual industrial customers that are, as stated in Sec. 368.105(3), "deemed to be just and reasonable and approved by the commission" would presumably place most, if not all, of the burden of risk on the transmission company. The assignment of risk to the transmission company rather than the "general body of ratepayers" is one of the key elements that would differentiate intrastate pipelines from local distribution systems.

c. Would Peninsula Pipeline expose themselves to claims of discriminatory treatment from applying different rates and charges, terms and conditions to its customers whose usage and operating characteristics are similar?

PPC Response: Sec. 368.105(2) of the NGTPIRA provides that it is the duty of the FPSC "to ensure that all rates and services" of any natural gas transmission company are "just and reasonable and are not unreasonably preferential, prejudicial, or unduly discriminatory." Even when a transmission company is negotiating rates with a customer the statute provides that an affidavit must be provided to the FPSC indicating that the negotiated 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...." The Act also provides that rates must be, "... consistent in application to each class of customers" and that the FPSC may treat two or more customers served as a single class if the FPSC, "... considers that treatment to be appropriate." PPC would intend to fully comply with the statutory requirements related to customer rates.

It should be noted, however, that it is quite rare for two industrial or large volume customers to exhibit the "same or similar operating conditions". Distribution systems typically group customers solely on the basis of annual gas consumption. The cost to provide service to a respective customer is dependent on many variables other than annual usage. Delivery pressure requirements, seasonal usage, load factor, requirements for firm vs. interruptible service, and future load growth considerations are among the many factors that distinguish one customer from another. In addition, it would be unusual to find the capital cost to extend service to one customer equal to that of another. If the capital cost is recovered in rates (rather than in lump sum or in a surcharge) it would be reasonable to expect that such rates would reflect the difference in investment cost.

To our knowledge there is nothing in the NGTPIRA that requires cost-based rates for negotiated agreements between willing parties. The Act appears to contemplate that a sophisticated large-volume gas user and the transmission company should be able to negotiate rates with relatively limited regulatory oversight. In the event the negotiation leaves either party aggrieved, the statutes provide ample authority for the FPSC to resolve the dispute.

FPSC Staff Question No. 6: Will Peninsula Pipeline be an Open Access Pipeline?

PPC Response: Yes.

FPSC Staff Question No. 7: Will Peninsula Pipeline pursue existing and/or potential customers that are located in an existing LDC's or municipal's territory?

PPC Response: PPC has no plan to actively solicit existing natural gas customers in an LDC's or municipal's service area. However, Sec. 368.105(6) F.S., states that, "A natural gas transmission company shall provide transmission access, subject to available capacity, on a basis that is not unreasonably preferential, prejudicial, or unduly discriminatory; however, a natural gas transmission company shall not be required to provide transmission access to a person at rates that are not just and reasonable. A natural gas transmission company shall construct any necessary pipeline lateral facilities and related facilities for interconnection with a customer if that customer agrees to fully compensate the natural gas transmission company for reasonable costs incurred."

In the event a potential customer currently served by a local distribution system requests service, PPC would evaluate the feasibility of providing service, and if feasible, submit a proposed service agreement to the potential customer. PPC would view large volume energy users currently using a fuel other than natural gas or constructing new facilities as potential customers, regardless of their location.

FPSC Staff Question No. 8: What, if anything, will prevent Peninsula Pipeline from encountering territorial disputes?

PPC Response: The referenced statutes are relatively clear on the FPSC role in resolving disputes between intrastate pipelines and other transmission companies or their customers. Sec. 368.105(6) states, "The commission shall resolve any controversy between the natural gas transmission company and a person desiring transmission access, including access availability, type of service, applicable rates, or interconnection costs."

It is less clear to PPC whether Florida statutes recognize territorial disputes between an intrastate pipeline and an alternate transportation service provider. It would seem unlikely that a dispute between an intrastate pipeline and an interstate pipeline would be resolved by state action. In the event an LDC or municipal system expressed a territorial concern over an intrastate pipeline project, PPC is not certain how such a claim would be resolved. Rule 25-7.0472 F.S. appears to provide the FPSC authority to resolve territorial disputes between gas distribution systems, not between distribution systems and transmission pipelines. Moreover, the FPSC has not historically interceded on behalf of an LDC or municipal system when large-volume customers elected to directly connect to a FERC-regulated interstate pipeline, even if the customer was an existing LDC or municipal account. The NGPSA does provide authority to the FPSC to undertake a need determination as part of the FDEP certification process for proposed transmission pipelines. However, such certification is not required for projects which are less than 15 miles in length or which do not cross a county line.

In any event, as noted in the response to Question No. 7, PPC has no plan to actively pursue customers that would trigger a dispute of any type with a distribution system.

FPSC Staff Question No. 9: On page 22, in section b, it states that under the Flexible Gas Service (FGS) provision, if an FGS customer converts to service from an intrastate pipeline, the general body of ratepayers will not be harmed. Please explain the reasons why it is believed that Chesapeake Florida Division's general body of ratepayers will not be harmed.

PPC Response: Any extension of facilities that is provided under the Chesapeake Florida Division's FGS tariff is deemed to be "below the line". That is, the Florida Division is at risk for all of the investment capital required to construct the facilities. None of the investment is recorded as rate base. In return for accepting all of the risk related to a FGS project, the tariff enables the Florida Division to exclude the revenues from the FGS customer from its "above the line" earnings. In the event a FGS customer terminates service prior to the recovery of its investment cost, Florida Division has no opportunity to recovery any of its loss from ratepayers. Given that the revenues from FGS customers do not contribute to the Florida Division's "above the line" earnings, the general body of ratepayers is unaffected by any increase or decrease in such revenues.

FPSC Staff Question No. 10: Currently, Chesapeake Florida Division serves two customers in Quincy, Florida. The service is provided by a lateral off the FGT pipeline system. Explain why Chesapeake Florida Division cannot continue this practice to fulfill the type "a" expansion addressed on page 12.

PPC Response: Chesapeake's Florida Division can, and presumably will, continue to provide service to industrial customers by constructing laterals off of interstate pipelines.

FPSC Staff Question No. 11: Does Peninsula Pipeline envision that it will interconnect with Chesapeake Florida Division distribution lines to serve end use customers?

PPC Response: PPC has no current plans to interconnect with Chesapeake's Florida Division. The statutes do not provide a clear distinction between the types of facilities that may be operated by LDCs as opposed to those that may be operated under the NGTPIRA and NGPSA by intrastate transmission companies. In its petition PPC offered several parameters within which Petitioner proposes to operate, in addition to statutory and rule requirements. As stated in paragraph No. 62 (b) of the PPC petition. "Existing regulated distribution system customers of Chesapeake, excluding customers served through the Flexible Gas Service tariff provision, would not be eligible for service through the intrastate pipeline, unless specifically authorized by the Commission."