

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF DELTA NATURAL GAS	)	
COMPANY, INC. FOR AN ORDER DECLARING	)	
THAT IT IS AUTHORIZED TO CONSTRUCT,	)	CASE NO.
OWN AND OPERATE A COMPRESSED	)	2013-00365
NATURAL GAS STATION IN BEREA,	)	
KENTUCKY	)	

ORDER

On October 3, 2013, Delta Natural Gas Company, Inc. ("Delta") filed an application for a declaratory order pursuant to 807 KAR 5:001, Section 19,<sup>1</sup> and KRS 278.508, permitting it to construct, own, and operate a compressed natural gas ("CNG") fueling station at its existing facilities on Glades Road in Berea, Kentucky, to fuel motor vehicles without the Commission's issuance of a Certificate of Public Convenience and Necessity ("CPCN") pursuant to KRS 278.020(1). In the alternative, Delta requested that it be granted a CPCN allowing it to construct a CNG fueling station. Delta further requested revisions to its tariff to establish rates and conditions for service to CNG fueling stations.

On November 4, 2013, the Commission established a procedural schedule which directed Delta to file testimony and provided for discovery on Delta. The Attorney General of the Commonwealth of Kentucky, through his Office of Rate Intervention ("AG"), and Interstate Gas Supply, Inc. and Clean Energy Fuel Corp. (jointly "CNG Parties") requested and were granted full intervention. On February 24, 2014, the

---

<sup>1</sup> Although Delta's application requests a declaratory order pursuant to 807 KAR 5:001, Section 18, the correct citation for an application for a declaratory order is 807 KAR 5:001, Section 19.

Commission amended the procedural schedule to provide for direct testimony and discovery on the CNG Parties and rebuttal testimony by Delta. The Commission held an evidentiary hearing on September 16, 2014, and Delta responded to information requests made at the Hearing by Commission Staff and the AG. Post-hearing briefs were filed by Delta, the AG, and the CNG Parties. The case now stands submitted for a decision.

### DELTA'S PROPOSED PROJECT

Delta is a Kentucky corporation and a local distribution company ("LDC") that purchases, sells, stores, and transports natural gas to approximately 35,000 consumers in 23 counties in Kentucky.<sup>2</sup> It also wholly owns three unregulated subsidiaries that are engaged in the purchase and sale of natural gas.<sup>3</sup> Delta's proposal is to construct, own, and operate a CNG fueling station ("CNG Station") at 129 Glades Road in Berea, Kentucky, on the same lot as Delta's Berea district office. Delta indicates this will be within close proximity to Interstate 75, U.S. 25, and Berea College in Berea, Kentucky.<sup>4</sup> Delta is requesting that the Commission approve construction and operation of the CNG Station as a pilot project,<sup>5</sup> which Delta states will provide both it and the Commission the opportunity to monitor the operations of a utility-operated CNG Station to determine

---

<sup>2</sup> *Annual Report of Delta Natural Gas Company, Inc. to the Kentucky Public Service Commission for the Year ended December 31, 2013* at 4. Delta serves the following counties: Bath, Bell, Bourbon, Clark, Clay, Estill, Fayette, Fleming, Garrard, Jackson, Jessamine, Knox, Laurel, Lee, Leslie, Madison, Mason, Menifee, Montgomery, Powell, Robertson, Rowan, and Whitley.

<sup>3</sup> *Id.* at 10. The three subsidiaries are Delta Resources, Inc., Delgasco, Inc., and Enpro, Inc.

<sup>4</sup> Application at 1. *See also* Direct Testimony of Jonathon W. Morphew ("Morphew Testimony") at 4; and Morphew Testimony, Exhibit 1.

<sup>5</sup> Delta's response to Commission Staff's First Request for Information, Item 5. *See also* Rebuttal Testimony of Matthew D. Wesolosky ("Wesolosky Rebuttal Testimony") at 6.

if the Commission should consider approving additional stations in the future.<sup>6</sup> Delta contends that there are significant public policy reasons why its proposal, which includes tax incentives offered by the state, should go forward as a model partnership between the state, the Commission, and the utility, to encourage Delta and other investor-owned utilities in Kentucky to build the infrastructure that will enable CNG to become a viable transportation fuel choice in Kentucky.<sup>7</sup> Delta states that the proposed CNG Station will provide citizens and businesses the opportunity to take advantage of CNG as a more cost-effective transportation fuel,<sup>8</sup> as CNG is currently plentiful and its price is stable. Delta also asserts that CNG is a clean alternative motor vehicle fuel, and its use reduces reliance on foreign oil.<sup>9</sup> Finally, Delta states that natural gas vehicles are safe, require less maintenance, and have a longer engine life than conventional vehicles.<sup>10</sup>

Delta advises that the CNG Station will provide natural gas as fuel for both passenger and commercial vehicles.<sup>11</sup> The station is proposed to be open 24 hours each day, seven days per week,<sup>12</sup> and would require no on-site Delta employees.<sup>13</sup> It would be equipped with two dispensers, each with two hoses and nozzles and two card

---

<sup>6</sup> *Id.*

<sup>7</sup> Brown Testimony at 3.

<sup>8</sup> *Id.* at 2.

<sup>9</sup> *Id.* at 5.

<sup>10</sup> *Id.*

<sup>11</sup> Morphew Testimony at 4.

<sup>12</sup> *Id.* at 6.

<sup>13</sup> *Id.* at 7.

readers, allowing CNG to be available to four vehicles simultaneously.<sup>14</sup> Access to the CNG Station would be provided by entry and exit driveways constructed of concrete or asphalt. A canopy equipped with electric lighting would facilitate 24-hour access for fueling.<sup>15</sup> Pricing and capacities would be indicated in gasoline gallon equivalent (“GGE”) on the dispensers and on signage provided in front of the station.<sup>16</sup>

Delta met with various vendors of CNG equipment and other utilities that operate CNG stations to arrive at the CNG Station’s proposed design. Delta’s projected construction costs and the equipment needed for the CNG Station are based on these contacts and meetings.<sup>17</sup> Delta estimates the cost to construct the proposed CNG Station at \$1,398,325,<sup>18</sup> which is higher than its original estimate of \$1,293,105.<sup>19</sup> Delta anticipates that it would finance construction of the CNG Station initially with internally generated cash and short-term debt,<sup>20</sup> which would ultimately be consolidated into its capital structure and funded consistent with Delta’s overall mix of debt and equity.<sup>21</sup> Delta proposes to treat the CNG Station as an addition to its utility rate base and to

---

<sup>14</sup> *Id.* at 5.

<sup>15</sup> *Id.* at 6. *See also* Morphew Testimony, Exhibit 1.

<sup>16</sup> *Id.* at 6.

<sup>17</sup> Direct Testimony of Matthew D. Wesolosky (“Wesolosky Testimony”) at 3. *See also* Direct Examination of Wesolosky, September 16, 2014 Hearing at 2:02:35-2:03:08, and Revised Exhibit 1.

<sup>18</sup> *Id.*, Revised Exhibit 1. *See also* Direct Examination of Morphew, September 16, 2014 Hearing at 3:12:00-3:13:39, and Delta Exhibit 3.

<sup>19</sup> Wesolosky Testimony, Exhibit I.

<sup>20</sup> Application at 4. *See also* Wesolosky Testimony at 3.

<sup>21</sup> Direct Examination of Wesolosky, September 16, 2014 Hearing at 2:03:08-2:05:00, and Revised Exhibit 1. *See also* Wesolosky Testimony at 3.

recover all expenses, including gas costs, associated with the operation of the CNG Station as part of its regulated revenue requirement in its next general rate case.<sup>22</sup>

Delta has applied to the Cabinet for Economic Development for certain tax incentives for its proposed CNG Station, pursuant to the Incentives for Energy Independence Act.<sup>23</sup> The proposed CNG Station will be eligible for up to \$250,000 of tax incentives related to sales tax, income tax, and severance tax, which, if received, will be used to offset the total project cost.<sup>24</sup>

Delta maintains that its proposed CNG Station, and its intent to include all costs and expenses in its rate base and revenue requirements, complies with the requirements of KRS 278.508.<sup>25</sup> Delta states that its proposed sale of CNG as a motor vehicle fuel, in accordance with KRS 278.508(1),<sup>26</sup> will not be regulated by the Commission,<sup>27</sup> which will give Delta the flexibility to set market-based prices that are

---

<sup>22</sup> Direct Testimony of John B. Brown ("Brown Testimony") at 7.

<sup>23</sup> KRS 154.27-020 (Aug. 30, 2007).

<sup>24</sup> Wesolosky Testimony at 6. *See also* Delta's response to Commission Staff's Post-Hearing Data Request, Item 2.

<sup>25</sup> KRS 278.508. Exemption of sale of natural gas used as a motor vehicle fuel from regulation—Regulation of transportation, distribution, or delivery of natural gas used as a motor vehicle fuel.

<sup>26</sup> KRS 278.508(1) states that:

Notwithstanding any other provisions of this chapter, the rates, terms, and conditions of service for the sale of natural gas to a compressed natural gas fuel station, retailer, or to any end-user for use as a motor vehicle fuel, shall not be subject to regulation by the Kentucky Public Service Commission. Any utility provider of such a nonregulated service shall keep separate records and books of account adequate to allow the commission to allocate costs and revenues and to perform other acts that will assist the commission in enforcing this section.

<sup>27</sup> Brown Testimony at 10.

competitive with other CNG stations as well as gasoline stations.<sup>28</sup> Delta states that it will keep separate records and books of account adequate to allow the Commission to allocate costs and revenues and to perform other functions that will assist it in enforcing this statutory section, as required by KRS 278.508(1).<sup>29</sup>

Delta intends to purchase natural gas for the proposed CNG Station from either local production or from third-party gas marketers,<sup>30</sup> and states that pursuant to KRS 278.508(2),<sup>31</sup> its transportation of natural gas to the proposed CNG Station will be subject to regulation by the Commission.<sup>32</sup> Delta intends to charge the proposed CNG Station pursuant to its Interruptible Service tariff and its Transportation of Gas for Others—On System Utilization tariff (“On System Transportation Tariff”) as if it were an unaffiliated customer,<sup>33</sup> which will allow Delta to evaluate the profitability of the station as if it were a separate commercial entity.<sup>34</sup> The same rates are also proposed to apply to other entities that build CNG stations in Delta’s territory.<sup>35</sup> Delta proposes that both

---

<sup>28</sup> *Id.* at 10.

<sup>29</sup> *Id.*

<sup>30</sup> *Id.* at 9.

<sup>31</sup> KRS 278.508(2) states that:

The transportation, distribution, or delivery of natural gas to any compressed natural gas fuel station, retailer, or any end-user for use as a motor vehicle fuel, shall continue to be subject to regulation by the Kentucky Public Service Commission. Upon request by the utility, the commission shall set flexible rates with other motor fuels. Price adjustment pursuant to these flexible rates is not rate changes for purposes of this chapter.

<sup>32</sup> Brown Testimony at 12.

<sup>33</sup> *Id.* at 11.

<sup>34</sup> *Id.*

<sup>35</sup> *Id.* at 12.

tariffs be amended to provide for the flexibility to compete with other motor vehicle fuels.<sup>36</sup> Specifically, Delta seeks to amend its Interruptible Service tariff to permit it to waive, at its sole discretion, the customer charge and Pipe Replacement Program charge for CNG fueling stations.<sup>37</sup> It also seeks to amend its On System Transportation tariff to permit it to negotiate, at its sole discretion, a fixed rate with CNG fueling stations, which will be no more than the maximum base rate and no less than the minimum base rate set forth in Delta's Interruptible Service tariff. Delta proposes to waive at its discretion the minimum volume requirement of the On System Transportation tariff for CNG fueling station customers.<sup>38</sup> Delta requests approval of its proposed tariff revisions regardless of the Commission's decision with respect to its proposed CNG station. Delta states that a non-affiliated CNG fueling station is in the process of becoming operational in Corbin, Kentucky, and that the proposed amendments to its tariff will allow that station and any others that come on Delta's system to compete with other motor vehicle fuels.<sup>39</sup>

Delta estimates that the annual operating expense for the CNG Station will be approximately \$20,000,<sup>40</sup> which includes electric service, dispenser repairs, compressor oil and filter changes, and natural gas filter replacements.<sup>41</sup> Delta maintains that these

---

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*, Exhibit IV.

<sup>38</sup> *Id.*

<sup>39</sup> Delta's Post-Hearing Brief at 14.

<sup>40</sup> Morpew Testimony at 8. *See also* Wesolosky Testimony at 3.

<sup>41</sup> Morpew Testimony at 8.

operating expenses will be reduced by Delta's own use of the station to fuel some of its company-owned vehicles and by making the CNG Station available to the public.<sup>42</sup>

Currently, Delta has no CNG vehicles, but states that once the CNG Station is in operation<sup>43</sup> and when Delta's fleet vehicles in the area surrounding the CNG Station require replacement, up to 11 of its gasoline vehicles will be replaced with natural gas/gasoline dual-fuel vehicles.<sup>44</sup> Delta has discussed the proposed CNG Station and the use of natural gas as a motor vehicle fuel with local entities having vehicle fleets, including Berea College and the city of Berea,<sup>45</sup> and representatives of both support Delta's proposal and will consider purchasing CNG vehicles in the future if the CNG station is approved.<sup>46</sup>

Delta did not conduct a detailed market analysis relating to its proposed CNG Station. It acknowledges that there are no fleets in its service territory that use CNG, that no other entities offer CNG for vehicle fuel in its service territory, and that there is no current market for CNG in its service territory.<sup>47</sup> Delta states that Honda, Ford, and Chevrolet all offer passenger and commercial use vehicles that are equipped for dual fuel operation and can use both CNG and gasoline.<sup>48</sup>

---

<sup>42</sup> Brown Testimony at 4.

<sup>43</sup> Morpew Testimony at 7.

<sup>44</sup> *Id.* See also Wesolosky Testimony at 4.

<sup>45</sup> Morpew Testimony at 7.

<sup>46</sup> Public Comment of Randy Stone, City Administrator, Berea, Ky., September 16, 2014 Hearing at 10:09:20-10:11:16. See also Public Comment of Lyle Roelofs, President, Berea College, September 16, 2014 Hearing at 10:06:31-10:08:43.

<sup>47</sup> Brown Testimony at 8.

<sup>48</sup> Morpew Testimony at 7-8.



Delta states that its proposal also complies with the requirements of KRS 278.508(3), and that the CNG Station will not adversely affect its costs or the availability of natural gas to its utility sales customers.<sup>49</sup> Delta confirms that the impact of construction and operation of the CNG Station, in total, will increase its annual revenue requirement by approximately \$234,900, including a return of \$158,000 on its investment, and increased annual expenses of \$76,900.<sup>50</sup> Delta estimates that if its proposed CNG station makes no sales other than those it expects to make to the CNG fleet vehicles it plans to purchase, the average impact on residential customers would be approximately \$2.85 per year,<sup>51</sup> which it describes as *de minimis*.<sup>52</sup>

#### LEGAL STANDARDS

Delta's application seeks a declaratory order, pursuant to 807 KAR 5:001, Section 19, and KRS 278.508, that it is authorized to construct, own, and operate a CNG station within the ordinary course of business.<sup>53</sup>

807 KAR 5:001, Section 19, provides:

(1) The Commission may, upon application by a person substantially affected, issue a declaratory order with respect to the jurisdiction of the commission, the applicability to a person, property, or state of facts of an order or

---

<sup>49</sup> KRS 278.508(3) states that:

The sales or transportation transactions described in this section shall not adversely affect the regulated utility's cost or costs, or the availability of natural gas to its utility sales customers.

<sup>50</sup> Delta's response to the AG's Post-Hearing Data Request, Schedule I. The \$76,900 consists of the estimated operating expenses of \$20,000, depreciation expense of \$46,145, and property taxes of \$13,515.

<sup>51</sup> *Id.*

<sup>52</sup> Delta's Post-Hearing Brief at 2.

<sup>53</sup> 807 KAR 5:001, Section 15(3).

administrative regulation of the commission or provision of KRS Chapter 278, or with respect to the meaning and scope of an order or administrative regulation of the commission or provision of KRS Chapter 278.

KRS 278.508 was specifically enacted by the Kentucky General Assembly to address the sale of natural gas to a retail fueling station or end-user for use as a motor fuel, and states:

- (1) Notwithstanding any other provisions of this chapter, the rates, terms, and conditions of service for the sale of natural gas to a compressed natural gas fuel station, retailer, or to any end-user for use as a motor vehicle fuel, shall not be subject to regulation by the Kentucky Public Service Commission. Any utility provider of such a nonregulated service shall keep separate records and books of account adequate to allow the commission to allocate costs and revenues and to perform other acts that will assist the commission in enforcing this section.
- (2) The transportation, distribution, or delivery of natural gas to any compressed natural gas fuel station, retailer, or any end-user for use as a motor vehicle fuel, shall continue to be subject to regulation by the Kentucky Public Service Commission. Upon request by the utility, the commission shall set flexible rates with other motor fuels. Price adjustment pursuant to these flexible rates is not rate changes for purposes of this chapter.
- (3) The sales or transportation transactions described in this section shall not adversely affect the regulated utility's cost or costs, or the availability of natural gas to its utility sales customers.

In the alternative to a declaratory order, Delta requests that it be granted a CPCN to construct, own, and operate a CNG Station, pursuant to KRS 278.020(1), which provides in part:

- (1) No person, partnership, public or private corporation, or combination thereof shall commence providing utility service to or for the public or begin the construction of any plant, equipment, property, or facility for furnishing

to the public any of the services enumerated in KRS 278.010,<sup>54</sup> except . . . ordinary extensions of existing systems in the usual course of business, until that person has obtained from the Public Service Commission a certificate that public convenience and necessity require the service or construction.

Pursuant to 807 KAR 5:001, Section 15 (2)(a), an application for a CPCN, requires that an applicant include “[t]he facts relied upon to show that the proposed new construction is or will be required by public convenience or necessity,” and must demonstrate both a need for such facilities or services and an absence of wasteful duplication.<sup>55</sup> The Commission has defined “need” as “a showing of a substantial inadequacy of existing service, involving a consumer market sufficiently large to make it economically feasible for the new system or facility to be constructed or operated.”<sup>56</sup> Wasteful duplication includes “[a]n excess of capacity over need . . . [and also] “an excessive investment in relation to productivity or efficiency, and an unnecessary multiplicity of physical properties . . . .”<sup>57</sup>

807 KAR 5:001, Section 15(3), provides that a CPCN “shall not be required for extensions that do not create wasteful duplication of plant, equipment, property, or facilities . . . and that do not involve sufficient capital outlay to materially affect the

---

<sup>54</sup> The services enumerated in KRS 278.010(3) that involve natural gas include: (b) “[t]he production, manufacture, storage, distribution, sale, or furnishing of natural or manufactured gas, or a mixture of same, to or for the public, for compensation, for light, heat, power, or other uses;” and (c) “[t]he transporting or conveying of gas, crude oil, or other fluid substance by pipeline to or for the public, for compensation.”

<sup>55</sup> *Kentucky Utilities Co. v. Pub. Serv. Comm’n*, 252 S.W.2d 885 (Ky. 1952).

<sup>56</sup> *Id.* at 890. “[S]uch inadequacy must be due either to a substantial deficiency of service facilities, beyond what could be supplied by normal improvements in the ordinary course of business; or to indifference, poor management or disregard of the rights of consumers, persisting over such a period of time as to establish an inability or unwillingness to render adequate service.”

<sup>57</sup> *Id.*

existing financial condition of the utility involved, or *will not result in increased charges to its customers*” (emphasis added).

## ARGUMENTS

### CNG Parties

CNG Parties agree with Delta that CNG is a promising vehicle fuel<sup>58</sup> and do not object to Delta’s competing in the CNG marketplace by building and operating a CNG station through an unregulated affiliate company for which the costs and risk of building and operating a CNG station are borne only by Delta’s shareholders and not its ratepayers.<sup>59</sup>

CNG Parties summarize their position in their Post-Hearing Brief, stating that Kentucky law does not allow for the approval of Delta’s application; that Delta is overstating the economic benefit and understating the risk to Delta’s ratepayers of building the CNG Station; and that vehicle refueling is not a “natural monopoly” business, but a competitive one whose development in Kentucky will be hindered if Delta’s proposal is approved.

CNG Parties reject Delta’s claim that its proposed CNG Station complies with Kentucky law, which expressly prohibits an LDC from utilizing ratepayer dollars to subsidize an unregulated business.<sup>60</sup> As KRS 278.508 clearly labels the sale of CNG

---

<sup>58</sup> CNG Parties’ Post-Hearing Brief at 9.

<sup>59</sup> *Id.* at 1.

<sup>60</sup> KRS 278.2201 specifically states that “[a] utility shall not subsidize a nonregulated activity provided by an affiliate or by the utility itself.” *See also* Delta’s Post-Hearing Brief at 2.

as a motor vehicle fuel as a nonregulated activity,<sup>61</sup> CNG Parties argue that Delta's request for ratepayer subsidization is in conflict.<sup>62</sup> CNG Parties further dispute Delta's reliance on the provisions of KRS 278.508 as support for its proposal, stating that "nothing in KRS 278.508" discusses or contemplates an LDC building or owning a CNG station; the statute merely indicates that *if* an LDC sells natural gas to a CNG station, the sale of that natural gas shall not be regulated" (emphasis in the original).<sup>63</sup> CNG Parties also oppose Delta's request for a CPCN to construct a CNG fueling station pursuant to KRS 278.020(1), which requires that a utility demonstrate that public convenience and necessity require the service or construction, as Delta has not demonstrated, nor could it demonstrate, that public necessity requires that a CNG refueling station be built in Berea, Kentucky.<sup>64</sup>

With regard to the questionable economic benefit and understated risk they see in Delta's proposal, CNG Parties question Delta's estimates of the costs involved in constructing the CNG station and purchasing natural gas vehicles for its own fleet, as well as the variable cost components it used in its analysis. CNG Parties estimate that, in order for Delta to break even and meet the revenue requirements of the CNG Station, Delta will need to sell 500,000 GGE or more annually, in addition to what it uses for its fleet vehicles, rather than Delta's estimate of 107,000 GGE.<sup>65</sup>

---

<sup>61</sup> KRS 278.508(1) states in relevant part: "[T]he rates, terms, and conditions of service for the sale of natural gas to a compressed natural gas fuel station, retailer, or to any end-user for use as a motor vehicle fuel, shall not be subject to regulation by the Kentucky Public Service Commission."

<sup>62</sup> CNG Parties' Post-Hearing Brief at 5.

<sup>63</sup> *Id.* at 4.

<sup>64</sup> *Id.*

<sup>65</sup> *Id.* at 8.

According to CNG Parties, because commercial fleets are currently the biggest users of CNG, a company intending to site a CNG station would first obtain firm commitments from a number of surrounding commercial fleets to use that station before it is ever built.<sup>66</sup> Since Delta has not obtained any fleet commitments,<sup>67</sup> other than from its own small fleet, CNG Parties argue that it will be extremely difficult for Delta to meet its projected revenue requirements.<sup>68</sup> CNG Parties emphasize that private entities are willing to invest in CNG stations that have a reasonable chance to be economically viable. CNG Parties referenced Delta's admissions that there are very few large commercial fleets likely to use the CNG Station, and the fact that no other company or entity (including Delta shareholders, the city of Berea, or Berea College) is willing to put its own capital at risk to invest in the CNG Station, and conclude that Delta's proposed CNG Station is not an economically viable project or a good investment without receiving significant subsidies from Delta ratepayers.<sup>69</sup> Allowing Delta to recover its proposed CNG station costs through its regulated rate base will discourage the development of a robust CNG marketplace in the long run, the CNG parties contend.

CNG Parties thus conclude that the application should be denied.

## AG

The AG contends that as a matter of first impression in Kentucky, Delta's proposal automatically strikes discord between the jurisdictional oversight of the

---

<sup>66</sup> Cross Examination of Mrowzinski, September 16, 2014 Hearing at 5:05:34-5:08:10. *See also* Cross Examination of Brown, September 16, 2014 Hearing at 11:16:43-11:18:42.

<sup>67</sup> Cross Examination of Brown, September 16, 2014 Hearing at 11:13:00-11:14:20.

<sup>68</sup> Direct Testimony of Dave Mrowzinski ("Mrowzinski Testimony") at 11.

<sup>69</sup> CNG Parties' Post-Hearing Brief at 9.

Commission and the fundamental intent of relevant Kentucky law.<sup>70</sup> It does this by offending traditional ratemaking policy; by contravening the letter and intent of KRS 278.508; by failing to meet the requirements for a CPCN under KRS 278.020; and by seeking to “place the construction costs, operating expense, and risk in the company’s regulated rate base and revenue requirement . . . on the back of ratepayers.”<sup>71</sup>

The AG also considers Delta’s proposal to be in direct opposition to the clear intent of the General Assembly to foster a competitive environment for CNG as a motor vehicle fuel,<sup>72</sup> and as such will “clearly create an anti-competitive advantage for Delta in the CNG marketplace.”<sup>73</sup> As applied, the AG views Delta’s proposal as having an adverse impact on its regulated operations, in violation of KRS 278.508(3), by Delta’s plan to increase its volumetric charge to ratepayers in order to recover over \$1.3 million in construction costs for the CNG Station.<sup>74</sup> Further, he notes that this rate impact will affect Delta’s customers living in the vicinity of Berea, as well as those residing well beyond Berea in the 23 counties that constitute Delta’s entire service area.<sup>75</sup> The AG particularly takes exception to Delta’s characterization of the rate impact as “merely asking for a ‘*de minimis*’ or ‘*immaterial*’ rate increase on the customer bills,”<sup>76</sup> (emphasis in the original) which will increase \$0.24 per month or \$2.85 per year for the average

---

<sup>70</sup> AG’s Post-Hearing Brief at 5.

<sup>71</sup> *Id.*

<sup>72</sup> *Id.* at 8.

<sup>73</sup> *Id.* at 9. *See also* Mrowzinski Testimony at 13.

<sup>74</sup> AG’s Post-Hearing Brief at 6.

<sup>75</sup> *Id.* at 6-7.

<sup>76</sup> *Id.* at 7.

residential customer.<sup>77</sup> The AG concludes that Delta appears to have given no valid consideration to the rate burden its customers already bear, which is higher than that of most other natural gas customers in the state,<sup>78</sup> and further states, “The plain language of KRS 278.508(3) prohibits any adverse impact upon the regulated utility’s costs, with no exception for a ‘*de minimis*’ or ‘*immaterial*’ impact” (emphasis in original).<sup>79</sup>

The AG agrees with CNG Parties that Delta’s request for a CPCN, pursuant to KRS 278.020, has failed to demonstrate that there is a demand and need for the CNG Station. Prior to a utility’s commencing construction of any new facility, KRS 278.020(1) requires that it first prove that the requested facility is required for public convenience and necessity, that there is a need for such facilities, and that there is an absence of wasteful duplication. The AG argues that Delta has not submitted any evidence to demonstrate that there is a current consumer market sufficiently large to make a CNG Station economically feasible, and hence has not proven that there is a “need” for a CNG Station in Berea, Kentucky.<sup>80</sup> The AG further argues that Delta’s interpretation of “need” as the need to sustain the environment and reduce dependence on foreign transportation resources is not supported by any authority,<sup>81</sup> and that by its own

---

<sup>77</sup> *Id.* at 4. See also Delta’s response to the AG’s Post-Hearing Data Request, Item 1 and Schedule 1.

<sup>78</sup> AG’s Post-Hearing Brief at 7.

<sup>79</sup> *Id.* at 8.

<sup>80</sup> *Id.* at 11-12.

<sup>81</sup> *Id.* at 13.



admissions, Delta has not conducted a market analysis, or any research at all, to determine if the CNG Station will ever be economically feasible.<sup>82</sup>

The AG supports the legislative intent of KRS 278.508 to expand CNG as a vehicular fuel in a manner that does not adversely impact ratepayers and that fosters competition.<sup>83</sup> In this respect, the AG is not opposed to Delta's building and operating a CNG Station as an unregulated enterprise through the use of shareholder funds, through the development of a public/private partnership with the city of Berea, or through the use of grant or other funding mechanisms.<sup>84</sup> The AG strongly objects, however, to Delta forcing captive ratepayers to fund the CNG Station. The AG agrees with the CNG Parties that the current proposal, if approved, would violate both KRS 278.508 and KRS 278.020 and, therefore, should be denied.

#### FINDINGS

Having reviewed the record in this proceeding and being otherwise sufficiently advised, the Commission finds that Delta's proposal to construct, own, and operate the CNG Station and to place the capital costs and associated revenues and expenses in rate base present unique issues that have not previously been addressed by the Commission. The reasonableness of Delta's request for a declaratory order, pursuant to 807 KAR 5:001, Section 19, should first be determined. KRS 278.020(1) requires that no utility begin the construction of any plant, equipment, property, or facility, except for ordinary extensions of existing systems in the usual course of business, until it has obtained a CPCN from the Commission. Whether the proposed project requires a

---

<sup>82</sup> Cross Examination of Brown, September 16, 2014 Hearing at 10:26:20-10:27:05.

<sup>83</sup> AG's Post-Hearing Brief at 15.

<sup>84</sup> *Id.*

CPCN hinges upon whether the project is deemed to be an ordinary extension of an existing system. Commission regulations define ordinary extensions as extensions that do not create wasteful duplication of plant and facilities, do not conflict with existing certificates or service of other utilities, do not involve sufficient capital outlay to materially affect the existing financial condition of the utility, or *will not result in increased charges to its customers* (emphasis added).<sup>85</sup> Delta has clearly stated its intent to recover its investment in and expenses relating to the CNG Station through rates charged to its general body of ratepayers when it files its next rate case. It also intends that its CNG station be profitable and that revenues exceed expenses to the point that its ratepayers realize benefit from its ownership of the CNG station. To the extent that: 1) the station's profitability depends on the development of a local market for CNG that does not currently exist and is outside the control of Delta, and 2) costs related to the station will be inevitable and unescapable, and 3) since those costs will be greater than the revenues generated from the CNG Station for the foreseeable future, it cannot be considered an extension in the ordinary course of business. Therefore, Delta's request for a declaratory order should be denied.

Delta's request is, in the alternative, for a CPCN for the CNG Station. As the applicant in this case, Delta bears the burden of proof<sup>86</sup> that "public convenience and necessity" require that Delta construct, own, and operate the CNG Station, and that it will not result in excessive or wasteful investment. The record in this case indicates that Delta knows of no existing CNG vehicles that would utilize the proposed CNG Station if approved, and that Delta is only able to speculate as to when a CNG market may

---

<sup>85</sup> 807 KAR 5:001, Section 15(3).

<sup>86</sup> *Energy Regulatory Commission v. Kentucky Power Co.*, 605 S.W.2d 46 (Ky. App. 1980).

develop in its service territory, even within its own fleet. The city of Berea, Berea College, and the Berea School Board have expressed interest in using CNG for their own fleets, but currently own no CNG vehicles and have made no firm commitments to purchase vehicles in the future. With no evidence that a CNG market exists or is likely to develop in the near future, the Commission is not convinced that the proposed CNG Station is needed or will be used to such an extent to make it an economic investment. The Commission finds that, as suggested by CNG Parties and the AG, Delta's stated goals of using natural gas as a clean alternative motor vehicle fuel and reducing reliance on foreign oil could be accomplished through one of its wholly owned unregulated subsidiaries, with the risk incurred by Delta's shareholders, rather than requiring subsidization by its ratepayers.

The Commission further finds that even if Delta's evidence had convinced us that there was a need for a CNG Station, the provisions of KRS 278.508 mandate that such a need be met not by a utility providing a regulated activity, but by the provider of a nonregulated activity. Delta claims that the proposed project meets the requirements of KRS 278.508(1) because Delta will keep "separate records and books of account adequate to allow the Commission to allocate costs and revenues." Delta's proposal, however, makes this claim disingenuous, as nothing in Delta's application suggests that keeping separate records and books of account is for the purpose of enabling KRS 278.508(3), which requires that the transactions described not adversely affect the regulated utility's cost or costs. As the AG points out, the plain language of KRS 278.508(3) prohibits any adverse impact upon the regulated utility's cost, with no exception for the magnitude of the impact. Additionally, KRS 278.2201 expressly

provides that “[a] utility shall not subsidize a nonregulated activity provided by an affiliate or by the utility itself.” Delta’s proposed sale of CNG for use as a motor vehicle fuel is an unregulated activity under KRS 278.508(1), and its proposal to include in rate base the costs of a nonregulated CNG Station directly violates the prohibition against cross-subsidation in KRS 278.2201.

The evidence clearly shows that it is Delta’s intent that its ratepayers will ultimately be responsible for any and all costs associated with the CNG Station. Delta’s claim that these costs will be *de minimis*, presumably based upon Delta’s proposal to spread the cost among its 35,000 customers, does not eliminate the adverse effect. It also raises the question of why these expected costs, if they are truly *de minimis*, are not being paid by Delta’s shareholders. Based upon Delta’s proposal, its shareholders will not share in the costs with Delta’s ratepayers, although they stand to benefit through the facility’s proposed inclusion in rate base. The reliance on rate base regulation to subsidize CNG used as a motor vehicle fuel in Kentucky raises the same concerns regarding anti-competitive activities that are expressed by the CNG Parties. For these reasons, the Commission finds that Delta’s request for a CPCN to construct, own, and operate a CNG Station and place the capital costs and associated revenues and expenses in rate base should be denied.

Despite the above findings that Delta’s application falls short of demonstrating the requisite need to construct, own, and operate a CNG Station as a regulated facility and that a CNG Station should not be funded by its ratepayers, the Commission commends Delta for its innovative proposal to use natural gas as a clean alternative motor vehicle fuel and to reduce reliance on foreign oil. Delta should be encouraged to

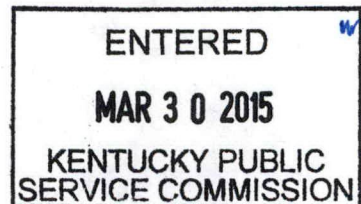
explore other funding mechanisms that do not involve utility customer subsidization to support a CNG Station in the future.

With regard to Delta's proposed tariff modifications to support future CNG fueling stations that may develop on its system, the Commission finds that they are reasonable and should be approved.

IT IS THEREFORE ORDERED that:

1. Delta's request for a declaratory order authorizing it to construct, own, and operate a CNG fueling station and to place the capital costs and associated revenues and expenses in rate base without the need for a CPCN is denied.
2. Delta's request for a CPCN to construct, own, and operate a CNG fueling station and to place the capital costs and associated revenues and expenses in rate base is denied.
3. Delta's request to modify its tariffs to enable sales to future CNG fueling stations is approved.
4. Nothing in this Order precludes Delta from constructing, owning or operating a CNG station without ratepayer subsidization.

By the Commission



ATTEST.

A handwritten signature in blue ink, consisting of several loops and a long horizontal stroke extending to the right.

Executive Director

\*Delta Natural Gas Company, Inc.  
3617 Lexington Road  
Winchester, KY 40391

\*Honorable Dennis G Howard II  
Assistant Attorney General  
Office of the Attorney General Utility & Rate  
1024 Capital Center Drive  
Suite 200  
Frankfort, KENTUCKY 40601-8204

\*Honorable Matthew R Malone  
Attorney at Law  
Hurt, Crosbie & May PLLC  
The Equus Building  
127 West Main Street  
Lexington, KENTUCKY 40507

\*Honorable Robert M Watt, III  
Attorney At Law  
STOLL KEENON OGDEN PLLC  
300 West Vine Street  
Suite 2100  
Lexington, KENTUCKY 40507-1801