COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF CHESAPEAKE APPALACHIA, L.L.C., PURSUANT TO KRS 278.485 AND 807 KAR 5:026, FOR ADJUSTMENT OF RATES FOR GAS SERVICE PROVIDED BY ITS FARM TAP SYSTEM	))))	CASE NO. 2010-00357

O R D E R

On September 7, 2010, Chesapeake Appalachia, L.L.C. ("Chesapeake"), submitted an application to increase its retail rate pursuant to KRS 278.485 and 807 KAR 5:026, the statute and regulation governing gathering systems that provide service to retail customers who tap onto such systems ("farm tap customers"). On September 14, 2010, the application was rejected for two filing deficiencies pursuant to: (1) 807 KAR 5:026, Section 9(1)(a), as Chesapeake had not given the Commission 60 days' notice of the proposed increase; and (2) 807 KAR 5:026, Section 9(1)(b), as the cost data provided to support the proposed increase was not current within 90 days of the date the proposed tariff was filed. On September 23, 2010, Chesapeake moved the Commission to accept as timely its filed cost data that was current as of May 2010 and to grant a deviation pursuant to 807 KAR 5:026, Section 10. Chesapeake also filed a tariff with a revised effective date of November 26, 2010 in order to provide the necessary 60 days' notice. The Commission's October 13, 2010 Order granted the motion for a deviation from 807 KAR 5:026, Section 9(b); found that the tariff filed on September 23, 2010 met the requirements of 807 KAR 5:026, Section 9(1)(a), curing the filing deficiency; and accepted Chesapeake's application for filing as of the date of that Order.

Chesapeake supplied additional information on October 22, 2010 in response to an information request by Commission Staff ("Staff"). There were no intervenors in this case.

BACKGROUND

KRS 278.485 requires every gas pipeline company obtaining gas from producing wells to provide service, upon request, to customers whose property is located within one-half air-mile of the company's producing gas well or gas gathering pipeline. Chesapeake has 515 such farm tap customers connected to 228 wells in Magoffin, Floyd, Letcher, Knott, Lawrence, and Perry counties.

Chesapeake states that, due to the increase in the cost of natural gas, it must adjust its farm tap rates, which have not been adjusted in 18 years. Chesapeake proposes the following increase in its farm tap rates:

	Current	Proposed	% Increase
All Mcf	$ 4.3292	$ 8.4899	96%

807 KAR 5:026, Section 9, allows a farm tap operator to request an adjustment in rates if: (1) the percentage change in rates does not exceed the percentage change in the price index during the most recent 12-month period immediately preceding the date the proposed tariff is filed;[1] and (2) the proposed rate does not exceed the highest average volumetric rate of a local gas distribution utility approved by the Commission and in effect on the date the proposed tariff is filed. Information provided by the Commission to Chesapeake prior to the initial filing of its application showed that the

[1] 807 KAR 5:026 defines price index as the average of the producer price index-utility natural gas (PPI-05) for the most recent 12-month period as published monthly by the United States Department of Labor, Bureau of Labor Statistics.

percentage change in the price index during the most recent 12-month period was a 2.3 percent decrease. Chesapeake's proposal for an increase of any amount would exceed a negative percentage change in the price index. Chesapeake's proposed rate does not exceed the highest average volumetric rate of a local gas distribution utility approved by the Commission.

Because Chesapeake did not meet the test of each of the two cited criteria, the regulation requires that it provide its costs to provide service during the previous two years, current within 90 days of the date the proposed tariff is filed. Chesapeake supplied an analysis of its administrative and proposed gas costs. It stated that it was using a 12-month New York Mercantile Exchange ("NYMEX") price strip for the period August 2010 through July 2011 and an Appalachian differential to calculate the gas cost portion of its rate. Chesapeake was requested to update its 12-month NYMEX strip to reflect a more current rate. The Commission notes that natural gas prices have been volatile since 2000 and finds that a rate based on NYMEX futures prices is more representative of current gas prices than a historical average. In prior farm tap cases, the Commission has approved this pricing mechanism as a reasonable proxy for the requirements of the regulation.[2] The Commission will continue to apply this method in determining the rate in this case.

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[2] Case No. 2009-00207, Application of Bear Fork Gas Company for Farm Tap Rate Increase (Ky. PSC Aug. 19, 2009); Case No. 2006-00460, Application of G.S. Knox Gas Company to Increase Its Rates and Charges for Providing Farm Tap Service Pursuant to KRS 278.485 (Ky. PSC Jan. 22, 2007); Case No. 2006-00122, Notice of Proposed Rate Change for Interstate Natural Gas Company (Ky. PSC Dec. 20, 2006).

Using information provided by Chesapeake, Staff calculated a $4.2688 per Dth 12-month NYMEX strip price for the period November 2010 through October 2011. Adding the average Appalachian differential of 20.29 cents that it had originally proposed, and adjusting for the heat content of the gas using Chesapeake's 1.2468 BTU conversion factor, produces a gas cost of $5.5753 per Mcf. Chesapeake proposed a gas cost of $6.4568 per Mcf.

For the 12 months ending August 2010, over one-third of Chesapeake's customers received free gas; these customers accounted for over one-half of the gas delivered to all of its farm tap customers. Chesapeake calculated the non-gas portion of its proposed rates by dividing the cost to serve all the customers for one year by volumes delivered to all customers for one year, although it receives revenues only from the paying customers. Even incorporating the lower gas cost of $5.5753, Chesapeake's proposed rate of $8.4899 will fall short of collecting the cost to serve all of its farm tap customers.

The Commission, having considered the evidence of record and being otherwise sufficiently advised, finds that the rate proposed by Chesapeake and included in the Appendix to this Order is fair, just, and reasonable, is in the public interest, and should be approved effective for service rendered on and after November 26, 2010.

IT IS THEREFORE ORDERED that:

1. Chesapeake's proposed rate is approved.

2. The rate in the Appendix attached hereto and incorporated herein is approved for service rendered on and after November 26, 2010.

3. Within 20 days of the date of this Order, Chesapeake shall file its revised tariff with this Commission showing the effective date, the date of issue, and a statement that it is issued pursuant to this Order.

By the Commission

ENTERED
NOV 23 2010
KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:

Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2010-00357 DATED NOV 23 2010

The following rates and charges are prescribed for the customers served by Chesapeake Appalachia, L.L.C. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

All Mcf	$ 8.4899

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