COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE TARIFF FILING OF COLUMBIA GAS OF KENTUCKY, INC. TO IMPLEMENT A SMALL VOLUME GAS TRANSPORTATION SERVICE, TO CONTINUE ITS GAS COST INCENTIVE MECHANISMS, AND TO CONTINUE ITS CUSTOMER ASSISTANCE PROGRAM	)	CASE NO. 99-165

O R D E R

On April 22, 1999, Columbia Gas of Kentucky, Inc. ("Columbia") filed an application for Commission approval to implement a small volume gas transportation service program ("Customer Choice"). Columbia also requested approval to continue its existing Gas Cost Incentive Program ("GCIP"),[1] and to continue its low-income Customer Assistance Program ("CAP").[2] The proposed Customer Choice program is designed to be effective for five years, from November 1, 1999 through October 31, 2004. The program is to be available to all Columbia customers with annual usage of less than 25,000 Mcf. It was the result of a collaborative process that included the Lexington-Fayette Urban County Government ("LFUCG"); the Community Action

[1] Case No. 96-079, The Tariff Filing of Columbia Gas of Kentucky, Inc. to Implement Gas Cost Incentive Rate Mechanisms, Orders dated July 31, 1996 and July 27, 1998.

[2] Case No. 94-179, Notice of Adjustment of Rates of Columbia Gas of Kentucky, Inc. on and after July 1, 1994, Orders dated November 1, 1994 and October 9, 1998.

Council of Fayette, Bourbon, Harrison and Nicholas Counties ("CAC"); and the Attorney General's Office ("AG").[3] Columbia also solicited and received input from FSG Energy Services, a marketing subsidiary of Wisconsin Public Service Resource Corporation.

Intervenors in this proceeding were LG&E Energy Corporation, LFUCG, CAC, United Gas Management, and Stand Energy Corporation ("Stand Energy"). After an informal conference on June 3, 1999, and three Commission Orders requesting additional information to which Columbia provided responses, a public hearing was held at the Commission offices on October 12, 1999. On November 12, 1999, briefs were filed by Columbia and CAC.

BACKGROUND

In September 1997, the Commission initiated Administrative Case No. 367[4] to explore issues related to the unbundling by Local Distribution Companies ("LDCs") of their existing bundled rates for natural gas service and the introduction of competition to the residential gas market. Columbia and the other major LDCs operating in Kentucky were participants in this proceeding as were marketers, public interest groups, and the AG. While the utilities and marketers were generally in favor of unbundling retail rates for natural gas service, low-income and residential customer groups expressed concerns about diminished reliability, as well as the significance of any real economic benefits that might be available in an unbundled, competitive market.

[3] Columbia's application indicated that LFUCG and CAC supported the proposed program while the AG took no official position on the proposal.

[4] Administrative Case No. 367, The Establishment of a Collaborative Forum to Discuss the Issues Related to Natural Gas Unbundling and the Introduction of Competition to the Residential Natural Gas Market.

The Commission found that any customer choice program proposed in Kentucky must address several issues in order to adequately protect the public interest. Those issues included: the obligation to serve; supplier of last resort; non-discriminatory access to offered services; codes of conduct for marketers and affiliates of regulated utilities; the prices (rates) for services; and billing of unbundled rates. The Commission also found that a definition of what constitutes a competitive marketplace would be of utmost importance because of the need to determine, on an ongoing basis, that a sufficient number of alternative and unaffiliated suppliers existed.

The Commission indicated that any utility proposing a customer choice or rate unbundling program would have to demonstrate that there had been sufficient input from its stakeholders. The Commission also emphasized the importance of consumer education as part of any such proposal and indicated that participating marketers, as well as utilities, would be expected to participate in the education process. Utilities were also informed that any proposed program should address certification of suppliers, transition costs, stranded costs, uncollectibles and disconnections, balancing requirements to maintain system integrity, and access to pipeline and capacity storage.

COLUMBIA'S CUSTOMER CHOICE PROGRAM

According to Columbia, the Customer Choice program is designed to address the issues set forth in the Commission's Order in Administrative Case No. 367.[5] It is a five-year program, designed to be effective November 1, 1999 through October 31, 2004. The major components of the program are as follows:

[5] Prepared Direct Testimony of Stephen L. Byars at 5.

- The program is to be available throughout Columbia’s service area to all customers with annual usage lower than 25,000 Mcf.

- The proposed small volume transportation rates are Columbia’s existing approved base, or distribution, rates, exclusive of its gas cost.

- Columbia is not proposing to exit the merchant function at this time.

- Columbia will serve as the supplier of last resort.

- Capacity assignment to gas marketers participating in the program is voluntary up to a certain level of customer participation (Phase I). At that point, which will be determined by Columbia, it may be mandatory (Phase II).

- Upon approval of the proposed tariffs, Columbia proposes a 60-day moratorium on marketer solicitation so that Columbia and the Commission, as well as the AG, LFUCG, and CAC, if they so desire, can conduct customer education efforts.

- Columbia proposes to certify marketers based on specific credit-worthiness standards set out in its proposed tariffs.

- Columbia proposes to establish a code of conduct for marketers, as well as standards of conduct for itself to address issues involving transactions with affiliates.

- Columbia proposes to continue to bill all customers, charging marketers 20 cents per account for the billing of the marketers’ Customer Choice customers. Columbia will assume the risk of collecting payment for gas commodity costs from Customer Choice customers and proposes to retain 2.5 percent of the marketers’ revenues as compensation for assuming this risk.

- Columbia proposes to implement a 35 cent per Mcf balancing charge for marketers that do not voluntarily take assignment of capacity.

- Columbia proposes to charge marketers 5 cents per Customer Choice Mcf volumes as a contribution toward stranded costs.

- Marketers must be able to provide firm service. Columbia may require a demonstration of a marketer's ability to reliably serve Customer Choice customers' gas requirements.

- Customers may enroll in the program by telephone, in writing, or by the Internet.

- Columbia will provide demand curves to marketers to better enable them to serve small customer groups.

- A marketer must enroll at least 100 customers or a customer group with minimum annual throughput of 10,000 Mcf in order to participate in the program.

- Columbia proposes to recover stranded costs through revenue opportunities identified as part of its application. Stranded costs are identified by Columbia as Gas Cost Recovery ("GCR") demand costs, information technology costs, consumer education costs, and lost standby revenues. Revenue opportunities are defined as marketer contributions, capacity assignment revenues, balancing charges, expiring contracts, sales customers' 65 percent share of off-system sales revenues, and sales customers' 65 percent share of capacity release revenues.

- If stranded costs exceed revenue opportunities over the five-year period of the program, Columbia proposes to absorb the first $3.0 million of the shortfall. The remaining shortfall would be collected using a method to be determined in the future. If revenue opportunities exceed stranded costs, Columbia proposes to retain the first $3.0 million in excess revenues and refund the remainder to customers.

- Columbia proposes to continue its current GCIP with no alterations other than to the capacity release benchmark and to use the customer portion of capacity release and off-system sales revenues as revenue opportunities to recover stranded costs.

- Columbia proposes to continue its CAP, with the CAC acting as aggregator and agent for customers that are CAP participants. These are the only customers for whom the Customer Choice program would be mandatory.

GOALS OF THE CUSTOMER CHOICE PROGRAM

Columbia identified six specific goals for the proposed Customer Choice program, which are as follows:

1. The program must provide an opportunity for customers to save money on their gas bills.

2. The program should provide marketers with as much flexibility as possible to provide customers savings by allowing marketers to serve customers using their own interstate pipeline capacity.

3. The program should be revenue neutral for Columbia and allow Columbia to recover its stranded costs and incremental program expenses.

4. The recovery of stranded costs must be as transparent to the customer as possible to permit the customer to make a clear and understandable choice between the marketer's offer and Columbia's sales rate.

5. Customers who choose to continue to purchase their gas supply using Columbia's traditional sales service should not incur any additional charges because of the implementation of the Customer Choice program.

6. Customer education is critical to the success of the program and customers must have an opportunity to learn about the program for a period of time before they begin to receive offers from marketers.

CASE PROCEDURE

The Commission, by Order dated May 18, 1999, scheduled an informal conference in this proceeding on June 3, 1999 for the purpose of discussing issues regarding Columbia's application. The principal reasons for the conference, as set forth in the Order, were to discuss the application's lack of a definition of a competitive marketplace and the question of cost justification for the proposed transportation service rates, as well as the other rates proposed by Columbia. The day of the informal conference, Columbia submitted a written response to the questions raised in the Commission's May 18, 1999 Order. Columbia provided a supplemental written response on June 18, 1999, which focused primarily on the cost justification issue.

In its written responses, in information responses, and at the hearing, Columbia maintained that the definition of a competitive marketplace was not an issue in this proceeding. Because it is not proposing to exit the merchant function at this time, and because sales customers can remain with Columbia or return from a marketer without restriction imposed by Columbia, it believes such a definition to be premature. In its prefiled testimony, Columbia stated that, "As long as Columbia remains in the merchant function with a regulated commodity rate the definition of workable competition is irrelevant."[6]

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[6] Prepared Direct Testimony of Kimra H. Cole at 8.

Columbia also stated that no cost justification was required for the use of its existing base rates as the small volume transportation rates. Since the Commission had approved those rates for sales service in Case No. 94-179, Columbia claimed that those rates, found to be fair, just, and reasonable by the Commission five years ago, were still fair, just, and reasonable.[7] In its supplemental response of June 18, 1999, Columbia set forth its position on the issue of cost support for its small volume transportation program rates, stating, "Columbia can find no basis on which to justify differing rates for delivery of gas under this program." Columbia concluded its response with, "Columbia respectfully requests the Commission to move past Staff's question regarding cost justification of the proposed transportation rates which are Columbia's approved base rates, and focus on the merits of the small volume gas transportation program." Although its existing base rates were the product of a unanimous settlement agreement in Case No. 94-179, Columbia indicated that it believed the rates to be cost-justified because they had been found to be fair, just, and reasonable by the Commission in its acceptance of that settlement agreement.[8]

REASONABLENESS OF THE CUSTOMER CHOICE PROGRAM

Columbia's proposed Customer Choice Program, as set out in Attachment B of its application, is generally acceptable to the Commission as a pilot program. Some modifications to the proposed program having to do with transition cost recovery will be required, however. The Commission is of the opinion that lost standby revenues should not be included with GCR demand costs, information technology, and education as a

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[7] Response to the Commission's July 2, 1999 Order, Item 11.

[8] Transcript of Evidence ("T.E.") at 51.

stranded cost. The Commission is further of the opinion that revenue opportunities should be comprised solely of capacity assignment revenues, balancing charges, marketer contributions, and off-system sales revenues. Revenues from expiring contracts and capacity release revenues should not be used to offset Customer Choice program stranded costs. Nor should the proposed $3.0 million deadband be used for excess revenues or costs. These issues are discussed in more detail later in the Order.

The program appears to ensure, to the greatest extent possible, that supply reliability to Customer Choice customers will not be threatened. Columbia will be the supplier of last resort, its own discontinuance of service rules will apply, and Columbia will perform the billing function for marketers. Therefore, customers should not be at risk of losing their gas supply due to marketer error or business failure. The program will have widespread availability, being offered to all small volume customers in Columbia's service area. Customers will have several enrollment options, which will facilitate the participation of those interested in doing so. The Commission is satisfied that these features of Columbia's proposed program will enable it and the Commission to draw conclusions as to the success of the program and the demand for small volume transportation programs. Such widespread availability will require a significant consumer education effort, for which Columbia and the Collaborative have made provision in the program.

The Commission is in support of the majority of the components of the Customer Choice program as proposed by Columbia, and endorses Columbia's stated goals for the program. In reference to the first of these goals, the testimony of Stand Energy indicated that savings were being achieved in jurisdictions where other Columbia

distribution companies have implemented similar programs.[9] Such testimony corroborates responses of Columbia to information requests which indicated the same. Despite some reservations regarding the issue of capacity assignment, the Commission can accept Columbia's more flexible approach of allowing marketers to take the capacity if they so choose, and charging a balancing charge if they don't. However, Columbia should be vigilant in determining when it is time to implement Phase II of the program. Phase II marks the point at which capacity assignment will be mandatory, and will mitigate the stranding of GCR demand costs. Such mitigation will lessen the need for continued revenue opportunities or some other method of cost recovery. Increased levels of capacity assignment to marketers will result in greater revenue opportunities to offset stranded costs. Columbia should notify the Commission prior to the time it decides to implement Phase II of capacity assignment.

Columbia's goal of sales customers not incurring any additional charges because of the Customer Choice program, while attractive in theory, is practically impossible to attain without impacting Columbia's revenues or charging exorbitant rates to marketers or Customer Choice customers. If this were not the case, Columbia would not have identified expiring contracts, off-system sales, and capacity release as revenue opportunities to offset stranded costs. Even if Columbia's proposed revenue opportunities do not result in "new charges" to sales customers, under Columbia's proposal, those customers would have to pay incrementally higher gas costs as a result of the program compared to what they would have paid absent the program. If the

[9] T.E. at 145-146.

Customer Choice program is ultimately beneficial, then recovery of costs associated with it (another of Columbia's goals) is legitimate.

It is because sales customers will have to bear a portion of the cost of the Customer Choice program that the Commission finds it necessary to require changes to Columbia's proposed transition cost recovery methodology as detailed in the Financial Model in Attachment A of the application. The Commission's revised transition cost recovery methodology will provide Columbia with an opportunity to recover approved stranded costs, although not to the extent proposed by Columbia. The total amount of stranded costs and revenue opportunities as modified and approved by the Commission are set out in summary form for the five-year period in Appendix A of this Order. A summary of the proposed and approved five-year amounts for stranded costs and revenue opportunities are set out in comparative form in Appendix A of this Order.

PROGRAM MODIFICATIONS

As stated earlier, the Commission finds that certain modifications related to transition cost recovery are necessary. These modifications are discussed in detail in the following paragraphs.

Stranded Costs and Revenue Opportunities

The Commission does not agree that all the stranded costs identified by Columbia should be included for recovery through the approved revenue opportunities. Lost standby revenues represent demand charges currently collected from commercial customers that directly offset sales customers' gas cost through Columbia's GCR mechanism. To the extent that these revenues decrease, the gas cost will be collected in its entirety from sales customers. The evidence supporting the need for this

particular cost to be offset by revenue opportunities is not persuasive. Lost standby revenues represent only $411,000, or 1.3 percent, of Columbia's total estimated stranded cost of $31,994,000 for the five years. This decrease in lost standby revenues could conceivably occur due to other changes in customers' circumstances, and is appropriate to be reflected through the GCR process.

The Commission believes the 5 cent marketer contribution toward stranded cost to be reasonable. However, a portion of revenues derived from marketer contributions should be designated to cover half of stranded costs attributable to education expenses. This is necessary to ensure that marketers participate equally in the customer education process initiated by Columbia.

The Commission also is not persuaded that expiring contracts and customers' share of capacity release and off-system sales revenues are appropriate methods to recover stranded costs as proposed by Columbia. Neither expiring contract revenues nor capacity release revenues should be used as revenue opportunities. Expiring contract revenues are generated by the decrease in demand charges associated with naturally expiring contracts. These contracts will no longer be needed because Columbia will no longer be required to arrange for the gas supply of Customer Choice customers. Capacity release revenues are attributable to the release of unneeded pipeline capacity to the secondary market during non-peak conditions. Because they reflect the cost of capacity necessary to serve only remaining sales customers, these are clearly savings in gas cost which should inure to the benefit of sales customers. Revenue opportunities represented by capacity assignment, balancing charges, and marketer contributions are understandable because they match costs to cost causers.

It is neither understandable nor reasonable for the sales customers' GCR mechanism to be adjusted as proposed to pay for stranded costs when that mechanism is reserved for actual levels of gas cost incurred on behalf of those customers. If a surcharge is eventually proposed and approved, and sales customers ultimately pay for transition cost recovery deficiency through a surcharge, they will have been provided the opportunity to know what they are paying for and the magnitude of the costs.

The Commission finds that total net proceeds from off-system sales, with the exception of operational sales, and not just the customers' gas cost incentive sharing portion of 65 percent as proposed by Columbia, should be used to offset stranded costs.[10] Historically, Columbia had not made off-system sales before its GCIP was approved. While offsetting sales customers' gas cost with the net proceeds from off-system sales revenues has certainly been beneficial to those customers, the Commission finds that using this non-traditional revenue source to partially fund Customer Choice program costs to be an even better use of these funds.

The evidence of record indicates that Columbia's earnings should not be adversely impacted so as to decline to an unreasonable level due to these decisions concerning stranded costs and revenue opportunities. In order to show the impacts of these decisions, the allowed stranded costs and revenue opportunities for the same time periods included in Columbia's financial model are shown in Appendix B to this Order.

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[10] The entirety of projected off-system sales are set out as the first note indicated by an asterisk at the bottom of the first page of Attachment A of Columbia's application.

Proposed Deadband

The Commission finds that the $3.0 million band on either side of actual stranded costs is not an acceptable method of addressing excess costs or revenues. Columbia's concern over implementing a surcharge should be sufficient incentive for it to minimize stranded costs. The evidence of record shows Columbia's earnings to be at a sufficiently high level that it would not be in the public interest to offer it the possibility of increased earnings via the proposed program. One of Columbia's stated goals in this proceeding is that the program be revenue neutral for Columbia, and allow it to recover 100 percent of its stranded costs and incremental program expenses. To allow the proposed $3.0 million deadband is counter-intuitive to the revenue neutrality objective. Unless cost recovery exactly matches stranded cost, which, for all practical purposes is impossible, the deadband would ensure that Columbia's revenues and earnings would be impacted by the implementation of the program. Any excess of cost or revenue will be addressed in the Commission's review of the pilot program. If the program continues, the revenue opportunity method approved by the Commission will either be continued or modified at that time, and a true-up mechanism may be instituted.

OTHER ISSUES

Customer Education

Columbia's goal regarding customer education is of paramount concern to the Commission. Although there is relatively little discussion in the record of this proceeding devoted to customer education, its importance to the ultimate success of the Customer Choice program cannot be understated. The Commission is satisfied that

Columbia is aware of the necessity of designing and implementing the best customer education program possible, and requests that Columbia share with it the details of that education program as they are developed. The 60-day moratorium proposed by Columbia is appropriate and will be useful for preparing customers for the opportunities inherent in choosing their own gas suppliers.

Definition of a Competitive Market and Cost Justification Issues

As previously stated, an informal conference was held at the Commission's offices on June 3, 1999 for the purpose of discussing the application's lack of a definition of a competitive marketplace and the question of cost justification for the proposed transportation service rates, as well as the other rates proposed by Columbia. Columbia's position on these issues has been discussed in the Case Procedure section earlier in this Order. Since the Commission has determined that the Customer Choice program will be a pilot program, for purposes of this Order the Commission can defer these issues while the program is in its initial stages.

The definition of a competitive marketplace does remain of concern, however, and the development of the small volume transportation market and the relative level of participation in it are not subjects that the Commission is willing to defer indefinitely. The Commission will consider the definition of a competitive marketplace essential to any proposed continuation of Columbia's Customer Choice program.

In support of the use of existing base, or distribution, rates as the proper rates for small volume transportation program service, Columbia has relied on the fact that other Columbia companies used their base rates in other jurisdictions and did not have to cost justify them for such use. Columbia also points out that the entire program is the result

of a collaborative process of the sort that was envisioned in the Commission's Order in Administrative Case No. 367 and that the Collaborative believes this approach to be reasonable.[11] The Commission commends Columbia and its Collaborative for their efforts that have produced a program that appears to address most of the concerns of the Commission raised in that Order. However, the use of a collaborative process, while ideal for developing program details that will be acceptable to the majority of affected market participants, does not mean that the statutory requirements for finding rates to be fair, just, and reasonable have been met.

Columbia has said when discussing other aspects of its proposal that it could not simply copy other programs but had to keep in mind its own customers and service area in formulating its program design. Likewise, the Commission cannot be content that, for whatever reason, other regulatory bodies accepted existing rates for the provision of a new service in their jurisdictions. The circumstances of different cases within this state are not identical, much less identical to those in other states. It was not the Commission's intent for its stated preference for a collaborative process to be interpreted as a blanket authorization for a proposed program created by a collaborative.

The Commission has concluded that the proposed program does have merit, and is pleased with the outcome of the collaborative process with a few minor exceptions. The progress of the program will need to be monitored, and Columbia itself has made provision for such monitoring in its proposal with its stated intention of filing an annual report; therefore, the Commission has few remaining reservations concerning the

[11] Prepared Direct Testimony of Steven R. Byars at 3.

security of supply to customers and the process that will be used to enlist and provide service to customers. However, to approve the program largely as proposed with the information available in the record, the Commission will have to accept for the pilot period Columbia's assertion that existing rates are representative of costs involved in supplying small volume transportation service. Existing rates may well be representative of costs during most of the initial five-year period, and incremental costs will in all likelihood be minimal. However, the Commission continues to be convinced that at some point cost shifts will cease to "net out." At that point, existing rates will not adequately represent either sales or Customer Choice service. The Commission believes that insufficient information exists to justify the use of existing base rates for the Customer Choice program indefinitely. However, since this is a pilot program, the Commission believes that the issue of cost justification for the use of its existing base rates as the small volume transportation rates and for the other proposed rates set out in Columbia's tariff can be deferred at this time.

Customer Choice Program – Three-Year Review

At the informal conference of June 3, 1999, it was conveyed to Columbia that the rates for Customer Choice program service should be transparent to customers.[12] By this, the Commission and Staff meant that rates should be representative of the costs to provide the service and that customers should understand what they are receiving in return for the rates they are charged. Columbia responded on two separate occasions that not everyone is well-versed in gas issues and terminology and rate-making

[12] One of Columbia's stated goals for the program is for the recovery of stranded costs to be as transparent as possible to customers.

methodologies. Apparently, this led Columbia to insist that using a surcharge methodology was inferior to its proposed revenue opportunity methodology to recover transition costs. Customers would be confused by a surcharge, according to Columbia. Therefore, the Collaborative concluded that the revenue opportunity method was better because it used the GCR mechanism to flow through the majority of stranded costs and offset them with certain gas cost revenues. This, according to Columbia, is a transparent methodology.

While it is true that most utility customers are not familiar with all the details of the provision of their utility service, the Commission believes it is crucial to design mechanisms that utility customers can identify and question if they so choose. This may very well be unattractive to customers, as Columbia alluded to in one of its responses. The filing of this program was driven by Columbia's desire to offer such a program to its customers; therefore, the lack of customer demand may cause customers to react negatively to a surcharge, if one is eventually proposed and approved. However, after the conclusion of the consumer education program conducted by Columbia, the Commission does not expect Columbia's ratepayers to be so uninformed that they would expect the Customer Choice program to be free of charge. If the Customer Choice program is beneficial to customers, keeping in mind the costs involved, then the recovery of costs associated with it is legitimate and need not be hidden.

In order for rates to be as transparent as possible at the earliest possible time, the Commission finds that a review of costs and rates should be initiated before the end of the proposed five-year program period. A period of three years is a suitable amount of time for the program to progress beyond its initial stages, for customer participation to

move at least past the introductory level, and for Columbia to gather preliminary information concerning costs involved in providing small volume transportation service relative to sales service. Because such information will be available at that time, the Commission will then begin the process of retaining an outside consultant, as authorized by KRS 278.255, to review all aspects of the Customer Choice program, to review the issue of a competitive marketplace, and to conduct a fully allocated cost-of-service study that will show what, if any, rates will need to be rebalanced in order to correctly represent costs to provide service.

In addition to the cost review process that will begin at the end of the three-year period and conclude prior to the end of the five-year pilot period, any necessary modifications to the program itself and approved financial model will also be considered. The cost recovery that has occurred through the acceptable revenue opportunities of capacity assignment, balancing charges, off-system sales, and marketer contributions will be reviewed, and a recommendation made as to whether this method of stranded cost recovery should be continued or modified. Once the consultant's review and report have been completed, the Commission will initiate a proceeding wherein Columbia and other parties may address the results of the consultant's report and other issues relating to the Customer Choice program as identified by the Commission at that time.

The Commission believes that the modifications contained in this Order more appropriately allow Columbia to meet its goals. As previously stated, the elimination of the $3.0 million deadband will ensure revenue neutrality, and modification of the revenue opportunities in combination with the cost review will ensure eventual transparency to customers as they compare Columbia's rates to those of marketers.

Marketer Issues

Marketers desiring to provide commodity services to consumers under the proposed small volume transportation tariff are required to meet certain eligibility requirements including credit worthiness standards and certain program threshold measures as set forth in the application at Section B, “Program Description.” In addition to those requirements, marketers are required to sign an aggregation agreement that establishes the marketers as agents of Columbia.

In Administrative Case No. 297[13] the Commission found it unnecessary to regulate brokers and dealers of natural gas. While the Commission found that such entities are engaged in arranging supplies of gas, it concluded that the market realities were such as to make these activities self-regulating. Columbia’s Customer Choice program, however, differs in material respects from the situation addressed in Administrative Case No. 297, particularly in that the proposed program is aimed toward residential consumers. Therefore, it is imperative that the Commission retain regulatory oversight over this program, and the necessity for such oversight is implicitly recognized in the proposed tariff filed by Columbia.

Columbia’s Customer Choice program requires that a natural gas supplier execute an Aggregation Agreement in order to enter the program, and also defines and limits the seller’s authority to supply the commodity. In addition, Columbia retains the authority to suspend or terminate a supplier’s participation in the Customer Choice program. To the extent that Columbia retains ultimate responsibility for the provision of

[13] Administrative Case No. 297, An Investigation of the Impact of Federal Policy on Natural Gas to Kentucky Consumer and Suppliers, Order dated May 29, 1987 at 21.

gas to customers pursuant to this program and retains control over the provision of gas by its agents, these agents lack the autonomy traditionally associated with a "utility" as defined in KRS 278.010. Further, Columbia's tariff requires its agents to file the information that would otherwise be required by the Commission pursuant to KRS 278.020. Accordingly, the question of whether agents of Columbia who market gas to residential consumers are "utilities" subject to full regulation by this Commission does not require a final decision herein. Pursuant to Columbia's tariff, both Columbia and its agents will remain answerable to the Commission as well as to the customers who receive service pursuant to the Customer Choice program. Under such an arrangement the Commission finds that its statutory directive to regulate utilities is fulfilled by its regulation of Columbia.

The Commission also takes notice of the Standard of Conduct and the Code of Conduct filed in the application at Section C, "Proposed Tariffs." The Commission is currently conducting its own investigation into the establishment of a Code of Conduct governing affiliated entities.[14] To the extent the Commission issues rules related to either affiliated entities or independent marketers, those rules once established will supersede the rules accepted in this pilot.

Columbia has proposed to file an Annual Report each year which will contain statistics detailing customer enrollment, participation, and related volumes; marketer participation; education activities; and stranded costs and revenue opportunities. For each participating marketer acting as agent for Columbia under the program, Columbia

[14] Administrative Case No. 369, An Investigation of the Need for Affiliate Transaction Rules and Cost Allocation Requirements for All Jurisdictional Utilities.

should also file with the Commission the marketer's name, address, telephone number, contact person, gas cost rates being charged to Customer Choice customers, and pricing and payment terms. This information should be filed not only with the Annual Report, but as often as necessary so that it is current and available for the Commission and for customers that call the Commission with questions regarding the program. Columbia had proposed to file its Annual Report by March 1 of each year. However, since the Commission's deliberations in this proceeding have pushed the program's starting date beyond that proposed by Columbia, the date for filing the Annual Report should be adjusted accordingly. Therefore, the due date for Columbia's Annual Report will be June 1 of each year, beginning June 1, 2001.

Continuation of the GCIP

Columbia has proposed to continue its GCIP which was approved by the Commission in Case No. 96-079. Columbia intends for the application in this proceeding to be considered by the Commission as a more comprehensive GCIP. The filing of a more comprehensive program was a prerequisite for further continuation of the program set out in the July 27, 1998 Order in Case No. 96-079.

Columbia's existing mechanism allows it to keep 35 percent of capacity release revenues after a certain historical benchmark has been achieved, as well as 35 percent of revenues resulting from off-system sales. Columbia has not achieved the established benchmark and, therefore, has not been able to share in capacity release revenues since the inception of the program. As of October 31, 1999, its sharing portion of completed off-system sales transactions was approximately $4.8 million.

By its application in the current case, Columbia proposes to continue its existing GCIP through October 31, 2004, coincident with the end of the proposed Customer Choice program. Other than a modification to the capacity release benchmark, Columbia proposes no changes to the GCIP itself. No expansion of its program to include gas cost commodity or transportation charges is contemplated. The most significant aspect of Columbia's proposal concerning the GCIP is that customers would lose their portions of capacity release revenues and off-system sales as offsets to their gas cost.

The disposition of capacity release revenues (100 percent to be used as an offset to gas cost) and off-system sales revenues (100 percent to be used as a revenue opportunity) has been addressed in the PROGRAM MODIFICATIONS section of this Order. The Commission finds it more appropriate that customers continue to experience an offset to their gas cost due to capacity release revenues rather than have these revenues used to offset Customer Choice stranded cost. The Commission further finds that the total amount of off-system sales is appropriate to use as a revenue opportunity to offset stranded cost rather than allowing Columbia to retain its portion while customers are required to forego theirs. In the absence of a more comprehensive GCIP involving additional elements of Columbia's gas cost components as contemplated by the July 27, 1998 Order, the continuation of the GCIP should be denied.

In its post-hearing brief, Columbia states that without the 35 percent sharing mechanism it could not justify the allocation of effort and resources necessary to complete off-system sales transactions. The Commission anticipates that Columbia will

consider stranded cost recovery to be sufficient incentive to continue to allocate the necessary effort and resources to off-system sales activities. Columbia's expressed concern over the possibility of charging a surcharge to its customers would be largely a moot point if it were able to generate sufficient off-system sales revenue to offset a majority of stranded costs.

Continuation of the CAP

Columbia is proposing to continue its CAP through the end of the five-year period proposed for the Customer Choice program. Columbia and the Collaborative have agreed that the CAP, which was originally approved as the result of a settlement among all the parties of Case No. 94-179, is benefiting those that the program is intended to assist and that it should continue in its current form. Columbia proposes that the CAP continue to be administered by the CAC, and that it will be funded through a $175,000 annual contribution from Columbia shareholders as well as the continuation of a charge on all residential, non-CAP volumes which will not exceed 1.5 cents per Mcf. The aggregation of the CAP participants' gas supply requirements by the CAC is intended to decrease the cost of serving CAP customers so that more low-income customers will be able to participate. Columbia will also be implementing recommendations based on its consultant's review of the initial three years of the CAP pilot concerning the administration of the CAP that are intended to make the program more cost-effective.

The Commission is concerned that the costs involved in the CAP out-weigh the benefits, as demonstrated in Columbia's application,[15] especially where ratepayers not

[15] Attachment G of Columbia's Application, Customer Assistance Program Consultant's Report at 14.

participating in the program are concerned. Therefore, the Commission finds that it is reasonable to continue the CAP as a pilot program for the time being and include it as an issue to be reviewed by the consultant retained to perform the Commission's three-year review. As stated earlier, the CAP was initially implemented as the result of a negotiated settlement in Columbia's most recent general rate case. In this instance, Columbia and the members of its Collaborative, most of which were signatories to that settlement, are proposing to continue the CAP, and included it as an integral part of the Customer Choice program. This will give the CAC an opportunity to pursue potential gas cost savings on behalf of these customers, which could translate into benefits for still more low-income customers than are currently being served by this program. The cost to ratepayers will not increase as the CAP surcharge will continue to be capped at 1.5 cents per Mcf, which is the upper limit the Commission imposed when it accepted the CAP pilot as part of the settlement in Case No. 96-179. Under these conditions, we believe extending the CAP pilot in order to observe the results of the administrative changes Columbia intends to implement and the interaction of the Customer Choice program and the CAP will be beneficial.

Tariff Modifications

All references to "marketers" in Columbia's tariffs should be changed to "agents."

Original Sheet No. 37f—Columbia should provide a more complete explanation of paying only 97.5 percent of revenues to marketers. Similar language should be inserted on page 4 of the Aggregation Agreement.

Original Sheet Nos. 37i through 37j are approved with the understanding that they may need to be amended following the Commission's decision in Administrative Case No. 369.

Seventh Revised Sheet No. 50 should be revised so that the Capacity Release Revenues section reads, "Capacity release revenues will be credited 100 percent to gas cost."

First Revised Sheet No. 51b should be modified to identify the CAP as a pilot program. The second sentence should be revised to read, "It is available to eligible residential customers …."

Original Sheet No. 58 should be modified so that Item 1, GCR Demand, correctly sets out the calculation of demand cost that will be stranded and charged to the Stranded Cost/Recovery Pool as set out in the testimony of Scott Phelps.

Original Sheet Nos. 58 and 59 should be modified to exclude Item 4, Lost Standby Revenues; Item 7, Expiring Contracts; and Item 9, (1), (2), and (3), Capacity Release. Item 8 should be modified to provide for the use of 100 percent of Off-system Sales revenues as opposed to 65 percent. Another item should be added so that revenues collected through the five cent per Mcf marketer charge are included in the recovery pool.

Original Sheet No. 59 should be modified to delete the paragraph below the Net Stranded Costs equation, and replace it with a statement that the recovery of net stranded costs, if any, will be addressed at the end of the pilot period.

SUMMARY

Having considered the evidence of record and being otherwise sufficiently advised, the Commission finds that:

1. Columbia's proposed small volume gas transportation program should be approved for a period of five years, from February 1, 2000 through January 31, 2005, subject to the modifications set out herein.

2. Columbia should inform the Commission of the progress of its customer education program development as such information becomes available.

3. Columbia should inform the Commission of the necessity of implementing Phase II of capacity assignment.

4. An external consultant should be retained to perform a review of the progress of the Customer Choice program and other issues in accordance with this Order.

5. Columbia should make the tariff modifications required herein.

6. Columbia's proposal to file an Annual Report with the Commission should be approved with the report to be filed no later than June 1 of each year.

7. Columbia should provide information concerning marketers acting as agents for Columbia as required herein. This information should be provided with its Annual Reports, and up-dated as frequently as necessary for such information to be current.

8. Continuation of the GCIP should not be approved and the associated tariff sheets should be withdrawn.

9. Continuation of the CAP should be approved effective February 1, 2000 through January 31, 2005.

IT IS THEREFORE ORDERED that:

1. Columbia's small volume gas transportation program is approved on a pilot basis effective February 1, 2000 through January 31, 2005.

2. Columbia's small volume gas transportation program shall be modified as required herein.

3. Within 30 days of the date of this Order, Columbia shall file tariff sheets subject to the modifications required herein.

4. Columbia shall inform the Commission of the progress of its customer education program development as such information becomes available. An initial advisory report shall be provided within 10 days of the date of this Order describing the status of the 60-day moratorium on marketer solicitation.

5. The Commission shall retain an external consultant to review the progress of the pilot program approved herein in accordance with the provisions of this Order.

6. Columbia shall inform the Commission of the necessity of implementing Phase II of capacity assignment.

7. Columbia shall file its Annual Report, as described in its application and with the further filing requirements as set out herein, by June 1 of each year. Columbia shall up-date the required marketer information as often as necessary.

8. Columbia's petition to continue its GCIP is hereby denied.

9. Columbia's CAP is approved to be continued as a pilot for a period of five years, effective February 1, 2000 through January 31, 2005.

Done at Frankfort, Kentucky, this 27th day of January, 2000.

By the Commission

ATTEST:

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Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 99-165 DATED JANUARY 27, 2000

A COMPARISON OF PROPOSED AND APPROVED STRANDED COSTS AND REVENUE OPPORTUNITIES FOR A PERIOD OF FIVE YEARS

Estimated Stranded Costs ($000)

	PROPOSED	APPROVED
GCR Demand	$ 30,973	$ 30,973
Information Technology	150	150
Education	460	460
Lost Standby Revenues	411	0
TOTAL	$ 31,994	$ 31,583

Revenue Opportunities ($000)

	PROPOSED	APPROVED
Capacity Assignment	$ 2,895	$ 2,895
Balancing Charges	6,443	6,443
Expiring Contracts	6,946	0
Off-System Sales	11,672	17,956
Capacity Release	2,904	0
Marketer Contribution	1,134	1,134
TOTAL	$ 31,994	$ 28,428
Revenue Excess (Deficiency)	$ 0	$ (3,155)

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 99-165 DATED JANUARY 27, 2000

APPROVED STRANDED COSTS AND REVENUE OPPORTUNITIES FOR THE PERIOD PROPOSED FOR THE CUSTOMER CHOICE PROGRAM ($000)

		Nov/Dec 1999	2000	2001	2002	2003	Thru Oct 2004	Total
STRANDED COSTS								
GCR – Demand	$	495	3,842	5,580	6,223	7,451	7,382	30,973
Information Technology		150						150
Education		250	50	20	20	50	70	460
Lost Standby Revenues		0	0	0	0	0	0	000
TOTAL	$	895	3,892	5,600	6,243	7,501	7,452	31,583
REVENUE OPPORTUNITIES								
Capacity Assignment	$	0	184	274	614	736	1,087	2,895
Balancing Charges		132	901	1,325	1,296	1,527	1,262	6,443
Expiring Contracts		0	0	0	0	0	0	000
Off-System Sales		780	4,024	3,670	3,566	3,360	2,556	17,956
Capacity Release		0	0	0	0	0	0	000
Marketer Contributions		19	143	210	231	273	258	1,134
TOTAL	$	931	5,252	5,479	5,707	5,896	5,163	28,428
NET STRANDED COSTS	$	(36)	(1,360)	(121)	(536)	(1,605)	(1,605)	(3,155)