COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

AN INVESTIGATION OF THE IMPACT OF FEDERAL POLICY ON NATURAL GAS TO KENTUCKY CONSUMERS AND SUPPLIERS	)))	ADMINISTRATIVE CASE NO. 297

O R D E R

During the 1970s, the United States faced an energy shortage in both oil and natural gas. Following the enactment of the Natural Gas Policy Act ("NGPA") in 1978, gas supplies became more plentiful but also more expensive. The NGPA established pricing formulas for the first sale of natural gas. As provided by Section 121, the price controls on certain categories of this gas were eliminated effective January 1, 1985.

In the past, the Federal Energy Regulatory Commission ("FERC") has approved various blanket certificates and special marketing transportation programs so that end-users (primarily industrial customers) could have access to lower cost gas supplies. However, in May 1985 the U.S. Court of Appeals, D.C. Circuit, found that blanket certificates and special marketing programs may be discriminatory in their availability and should be eliminated as of October 31, 1985.

On October 9, 1985, the FERC issued a Final Rule in Docket No. RM85-1-000, Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol. The rule provides that any pipeline voluntarily making itself a transporter of natural gas must offer non-discriminatory, open-access to its pipelines. The FERC's goal of this landmark decision is to give natural gas consumers more options for gas supplies. To the extent pipelines choose to participate, consumers and local utilities will be able to shop around for the cheapest and most reliable gas supplies. At the same time, producers gain access to pipeline capacity to market their supplies directly to consumers, distribution companies, and new markets.

The responsibility of determining much of the administration of this rule has been left to the states. Kentucky has a number of statutes that affect the authority of the Commission in this new environment. (See Appendix A) There may be a need for new laws in view of the FERC's policies.

At this time, Kentucky's five largest local distribution companies ("LDCs") have tariffs in place that allow some transportation of natural gas and new tariffs have been proposed. LDCs face competition not only from alternate fuels but also alternate supply arrangements. The potential shift of traditional customers with firm and interruptible sales to transportation arrangements could greatly affect both the LDCs and their remaining captive customers.

The effects of the aforementioned activities must be thoroughly analyzed since state regulatory commissions are being forced to reassess regulatory policy. The Commission is of the opinion that the appropriate forum for this analysis and discussion is a generic proceeding.

The Commission's overall goal is to develop a consistent and clear policy that will balance the interests of captive customers, and Kentucky distribution companies in light of federal regulations. The Commission understands that trade-offs between competing interests will be necessary. In initiating this investigation the Commission is seeking comments from the widest variety of viewpoints as it considers regulation to meet its objectives in light of the FERC's continued efforts to deregulate natural gas pipelines after partial wellhead decontrol. The Commission's objectives are as follows:

- To ensure that all customers of an LDC have the opportunity to benefit from increased competition in the natural gas industry.

- To maintain the economic and financial viability of the natural gas distribution industry in Kentucky.

- To expand the Commission's oversight of natural gas acquisition practices by LDCs.

- To examine the Commission's authority in fulfilling its mandate to assure just and reasonable rates for natural gas customers in Kentucky.

- To examine the extent to which LDCs should offer a variety of services to keep large volume end-users on their systems.

- To encourage the economic use of natural gas produced in Kentucky.

To aid in its analysis of the responses that will result from this Order, the Commission finds that **Columbia Gas of Kentucky, Inc., Delta Natural Gas Company, Inc., Louisville Gas and Electric Company, The Union Light, Heat and Power Company,** and **Western Kentucky Gas** shall supply the following descriptive data within 20 days of the date of this Order. **Interstate transmission companies** are asked to respond to the extent applicable within the same 20 days.

1. Identify your major gas suppliers and the following provisions of your supply contracts: term, price determination clause, take-or-pay/minimum bill, dedicated volumes, "out" clauses.

1a. Provide data to indicate the volume of intrastate and interstate gas in your supply, the cost per Mcf by major supplier and the system average cost per Mcf for the years 1980 through 1985. Explain any significant changes.

1b. Provide projections for the same factors through 1990, if available, and describe the assumptions used to develop the projections.

2. Provide data on how your sales volume has changed since 1980 by customer class and by usage. Explain any significant changes.

2a. Provide data on your sales volume projections through 1990, if available, and describe the assumption used to develop the projections.

3. Estimate the number of large volume customers, the volume of sales and associated revenues that have been lost to alternate supplies or fuels during the last 5 years.

3a. Provide projections for the same factors through 1990, if available, and describe the assumptions used to develop the projections.

4. Provide information on any programs that you have initiated to maintain your market share or regain large-volume customers. Summarize the effectiveness of these programs. Describe any programs that you intend to implement for these purposes during the next 5 years.

5. Provide information on the percentage change in rates by customer class since 1980. Explain any significant changes.

5a. Provide information on projected changes in rates by customer class through 1990, if available, and describe the assumptions used to develop the projections.

6. What are the "peak" and "normal" deliverability capabilities of your system during summer operations and winter operations? This information must be presented in a pipeline grid format at an appropriate scale for your system and must be broken down into the different areas, or sections, in which your system is divided. (See Appendix B for example.)

7. What is the maximum operating pressure ("MOP") and maximum allowable operating pressure ("MAOP") of your system for each area, or section, as presented in the pipeline grid(s)?

8. If you are requested to transport gas for an end-user, how will you determine if your system can accept the gas?

9. At present are there points along your system where an interconnection with another pipeline could not be made (for purposes of accepting "transportation" gas) due to pressure and/or volume limitations?

Other Kentucky distribution companies subject to the Commission's jurisdiction shall supply responses to descriptive questions 1, 1a, 2, (omit 2a), 3, (omit 3a), 4 and 8 above within 20 days of the date of this Order.

All other parties in this proceeding are asked to supply the Commission with a statement of position and a description of operations that includes the general nature of their gas acquisition practices (i.e., long- vs. short-term contracts and fixed volume vs. as available supply) within 20 days of the date of this Order. Any large-volume user who has switched to an alternate fuel or an alternate supply should briefly describe the factors that led to the decision to switch and the advantages and disadvantages to using the alternate.

The Commission finds that within 45 days of the date of this Order, **Columbia Gas of Kentucky, Inc., Delta Natural Gas Co., Louisville Gas and Electric Company, The Union Light, Heat and Power Company, and Western Kentucky Gas** shall respond to the following questions and are directed to pose any additional questions or submit comments on other topics that may be relevant to this investigation. The following **interstate transmission companies** are strongly encouraged to address the same questions and supply responses within the same 45 days. American Natural Resources, Columbia Gas Transmission Corp., Columbia Gulf Transmission Co., Indiana Utilities Corporation, Kentucky-West Virginia Gas Co., Midwestern Gas Transmission Co., Ohio River Pipeline Corporation, Tennessee Gas Pipeline Company, Texas Eastern Transmission Corp., Texas Gas Transmission Corp., and Trunkline Gas Company. **Other Kentucky distribution companies, intrastate pipelines, producers, and end-users** or their representatives are also invited and encouraged to submit responses to the following questions within 45 days of the date of this Order.

10. What will be the short-term and long-term impacts in Kentucky of the federal policy changes in the natural gas industry in the following areas?

a. Your operations, including costs and revenues.

b. Your natural gas acquisition practices.

c. Additional staff and expertise necessary for your operation.

d. Rate level and rate design.

e. Reliability of supply.

f. Customer load.

11. Given the federal policy changes, do you support or oppose the following: Explain.

a. State regulation of rates of affiliated entities. (i.e., gas production/brokerage/distribution transactions)

b. State regulation of rates of intrastate pipelines.

c. State regulation of rates of in-state production.

d. Issuance of a certificate of convenience and necessity by the Commission for construction activities of affiliated entities.

e. Issuance of a certificate of convenience and necessity by the Commission for construction activities of intrastate pipelines.

f. Issuance of a certificate of convenience and necessity by the Commission for construction activities of in-state producers.

12. Do you support or oppose the following? Explain.

a. Granting LDCs a service area.

b. Restricting construction of distribution facilities to LDCs.

c. Requiring Commission approval for all gas distribution construction.

d. Placing the burden of proof on utilities to show they cannot transport natural gas.

e. Modifying a utility's obligation to serve.

13. Do you support or oppose bypass of the LDC? Explain.

a. How will LDCs be affected?

b. To what extent do the LDCs have an obligation to serve?

c. What should be the priority on allocating transportation and supply capacity of the LDC among customers?

d. What risks are inherent to the end-user that chooses to bypass its LDC?

e. Should the Commission have a regulatory obligation to by-passers? Explain.

14. What is the impact of the current natural gas transportation tariffs on Kentucky ratepayers?

a. Does the impact vary by rate class?

b. Do current transportation tariffs encourage bypass of the LDC as supplier? As a transporter?

15. Should natural gas rates be unbundled? (i.e., supply and transmission services priced separately)

a. What variety of supply and transportation services should be offered? Why?

b. What services, if any, of these should be billed separately?

c. To what extent should LDCs rates be cost-based?

d. How should fixed costs be allocated between supply and transportation customers?

e. What services would a cost-of-service based transportation rate include?

f. What are effective ways of communicating price signals in a competitive natural gas market?

g. The Commission currently allows flexible pricing in natural gas retail and transportation rates to meet competition from alternative fuels. Should the Commission continue or expand this practice? Explain.

16. What is the impact of current natural gas acquisition practices on Kentucky ratepayers?

a. Does this impact vary by customer class?

b. What factors should the Commission consider in evaluating gas acquisition practices by LDCs?

c. Should the review of acquisition practices in purchased gas adjustments change as a result of federal policy changes? Why or why not?

17. What barriers, if any, exist to greater use of natural gas produced in Kentucky?

a. How will the federal policy changes affect the use of natural gas produced in Kentucky?

b. In what ways will use of natural gas produced in Kentucky benefit ratepayers?

c. What recommendations would you propose to increase the use of natural gas produced in Kentucky?

18. Should the Commission encourage competitive markets in natural gas supply? In transportation services? Explain.

a. What factors limit LDCs participation in competitive natural gas markets?

b. What factors limit large volume end-users participation in competitive natural gas markets?

c. Should the statutory definition of a public utility be modified in light of competition?

19. How will small LDCs be affected by the federal policy changes?

a. Will small LDCs be able to use alternate suppliers to achieve a lower average cost of gas?

b. Will small LDCs be able to offer a variety of supply and transportation services and remain financially viable? Why or why not?

c. What methods can the small LDCs use to place more pressure on their wholesale suppliers to obtain a lower average cost of gas?

d. Is formation of natural gas cooperatives by small companies to purchase natural gas a viable alternative?

e. How will the role of the wholesale suppliers of the small LDCs change as a result of the federal policy changes?

IT IS HEREBY ORDERED that:

1. This investigation be instituted and that all natural gas utilities under the Commission's jurisdiction shall be made parties to this proceeding. Moreover, the Commission urges other interested parties to participate in this proceeding to insure a full investigation.

2. All regulated natural gas utilities shall publish a one-time notice of this proceeding in a newspaper of general circulation in their service area and shall notify their large volume commercial and industrial users by letter. The prescribed notice is set out in Appendix C to this Order. The utility shall make copies of this Order available to interested parties.

3. All parties to this proceeding shall comply with the findings of this Order. An original and 10 copies of written responses shall be filed within the specified time frames. Each party shall make copies of its comments available on request.

4. Hearings shall be held in the Commission's offices in Frankfort, Kentucky, beginning at 9:00 A.M., April 1, 1986, for the purpose of receiving comments from regulated utilities and all other interested parties.

Done at Frankfort, Kentucky, this 17th day of January, 1986.

PUBLIC SERVICE COMMISSION

Richard D. Heman, Jr.

Chairman

Vice Chairman

Commissioner

ATTEST:

Secretary

Appendix A

LIST OF APPLICABLE STATUTES

KRS 278.101(3)(b) & (c) - Definitions

KRS 278.040 - Public service commission; jurisdiction; regulations

KRS 278.272 - Consideration of natural gas purchasing transactions in determining just and reasonable rates; limitation of authorized rate of return for natural gas operations

KRS 278.274 - Review of natural gas utility's purchasing practices in determining reasonableness of proposed rates, reduction of rates by commission

KRS 278.470 - Companies transporting oil or gas by pipeline are common carriers

KRS 278.480 - Pipeline companies may deliver oil or gas on order of person in possession

KRS 278.485 - Gas pipeline company to furnish gas; when; rates; duty of person applying for gas service and gas pipeline company; abandonment of gas wells; discontinuance of service

KRS 278.490 - Transportation of oil or gas received from connecting lines

KRS 278.504 - Definitions for KRS 278.505 to 278.507

KRS 278.505 - Transportation of natural gas in intrastate commerce by pipelines or local distribution companies with unused excess capacity

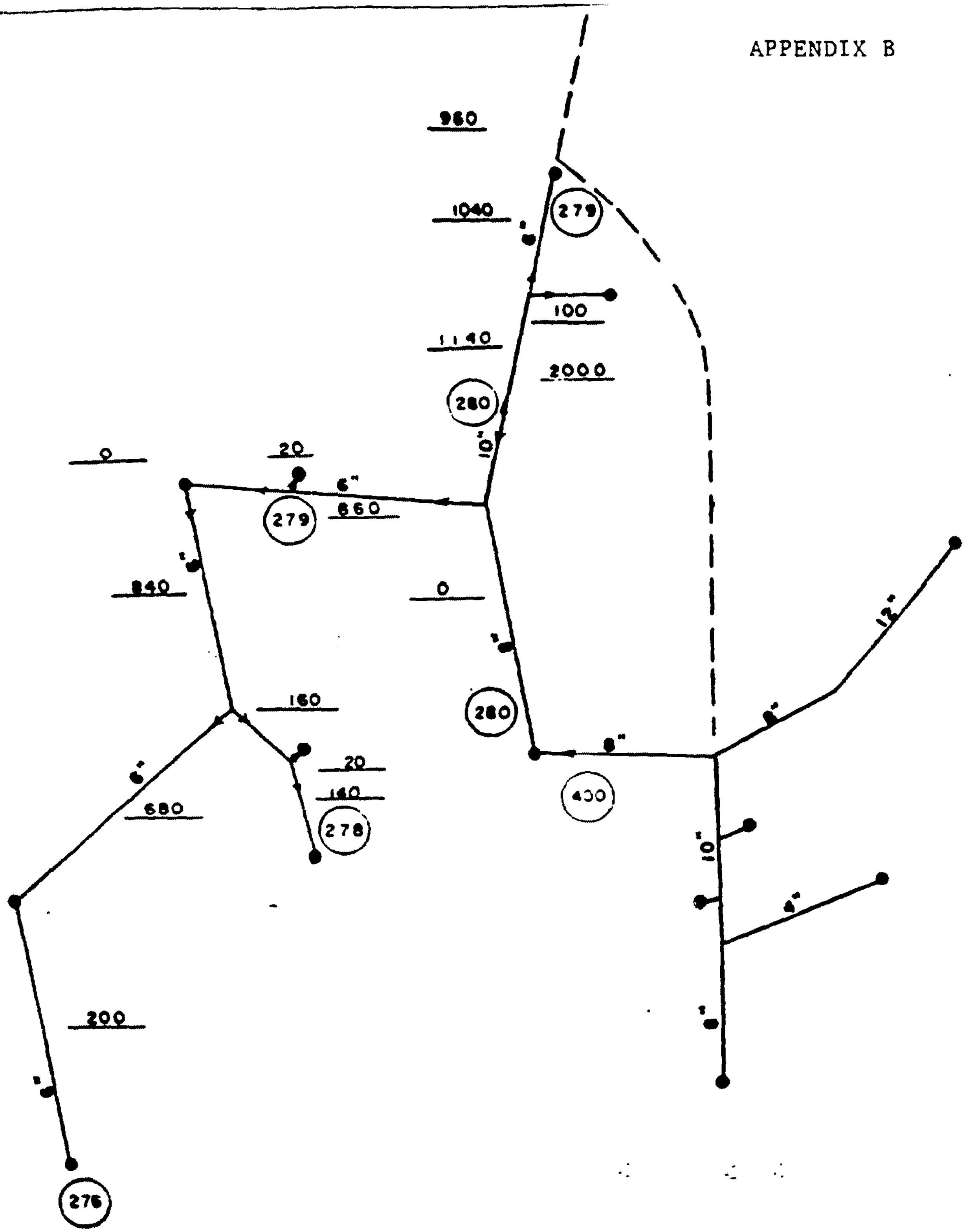
KRS 278.506 - Gas to meet pipeline quality standards; delivery and curtailment provisions

KRS 278.507 - Public service commission's policy to facilitate grater use of natural gas produced in Kentucky; commission's duties and prohibited activities

KRS 278.990 - Penalties

KRS 278.992 - Civil penalty for certain pipeline violations

APPENDIX B



MCFD

PSIG

PIPELINE GRID FOR ABC GAS Co.
EAST SECTION

EXHIBIT "1"

AVERAGE SUMMER CONDITIONS

SCALE: NONE | DATE:

APPENDIX C

NOTICE

The Public Service Commission will hold a hearing at 9:00 a.m., April 1, 1986, for the purpose of reassessing its policies as they relate to natural gas issues. The purpose of the hearing is to receive comments from all natural gas utilities, their customers and other interested parties, on matters related to natural gas supplies, transportation, competition and scope of regulation. Any person interested in filing comments can obtain a copy of the order from __________________________ at its offices located _________________________________ from _____ a.m. to _____ p.m., or by writing the Secretary of the Public Service Commission, 730 Schenkel Lane, Frankfort, Kentucky 40601.