

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

PETITION OF AUXIER ROAD)	
GAS COMPANY FOR APPROVAL)	
OF A CERTIFICATE OF)	CASE NO. 2001-069
CONVENIENCE AND NECESSITY)	
TO CONSTRUCT FACILITIES)	
AND SPECIAL CONTRACT)	

O R D E R

On April 6, 2001, Auxier Road Gas Company, Inc. ("Auxier") filed an application for a Certificate of Public Convenience and Necessity to construct a \$285,100 extension to its natural gas distribution system in Martin County, Kentucky and for approval of a special contract with the Federal Bureau of Prisons ("BOP"). This project consists of the construction of a natural gas pipeline and related appurtenances to provide natural gas service to a United States Penitentiary that the BOP is constructing in Martin County. The application stated that the proposed construction is to be financed with funds provided by Auxier; therefore, no approval of financing was requested.

Auxier proposes to install 11,300 feet of 6-inch, high density polyethylene plastic pipe (PE 2408 DR 11) from a connection at the gathering facilities of Columbia Natural Resources, Inc. ("CNR") to BOP's point of service at the prison. Auxier filed an agreement with CNR for gas sales and delivery service for a period of 5 years from October 1, 2001, for a maximum flow rate of 1,100 decatherms per day. CNR will install a pressure reducing station and metering facilities to provide natural gas at 50 pounds per square inch gauge pressure ("psig"). Auxier plans to install a gas meter with a

maximum capacity of 43.7 thousand cubic feet per hour ("Mcf/hr") at 50 psig. Auxier will further reduce the gas pressure at the BOP point of service to 15 psig. Auxier's contract with the BOP calls for an estimated maximum natural gas demand of 44.862 Mcf/hr and an estimated annual demand of 50,000 Mcf, of which 18,000 Mcf will be firm and 32,000 Mcf will be interruptible. The BOP also requires that the quality of gas furnished by Auxier meet specific quality standards set out in the gas sales agreement.

On May 8, 2001, Staff issued a request for information to which Auxier responded on May 18, 2001. Staff and representatives for Auxier participated in an informal conference on May 22, 2001. As a result of that conference, Auxier supplied additional information on June 20, 2001. Staff and Auxier participated in a telephone conference on July 3, 2001. Auxier supplied additional information requested by Staff by facsimile the same day.

Based upon the information provided in the application and the additional evidence of record, the Commission has concerns about the quality of gas that Auxier proposes to furnish the BOP. The proposed gas supply is raw, unprocessed gas from CNR's gathering system that, according to the analysis provided, is saturated with water vapor. Auxier plans to install a natural gas dryer, type PLD30-2.5, manufactured by Van Air Systems, Inc., Lake City, Pennsylvania. The proposed dryer contains desiccant that will reduce the water content to 25.3 pounds per million cubic feet ("MMcf") of natural gas; however, Auxier's agreement with BOP requires that the natural gas supplied contain less than 7 pounds of water per MMcf. In addition, the dryer is designed for a maximum flow rate of natural gas at 450 Mcf per day at 50 psig, while the BOP contract specifies that its maximum demand flow rate will be approximately 1,000 Mcf per day.

Auxier stated that, based on its own estimate of the flow to BOP and on its own experience with dryers, the proposed dryer would be sufficient.

Notwithstanding Auxier's assurances, the Commission is concerned that the gas delivered to BOP's point of service may not meet the quality standards included in the gas sales agreement. Because of its concern, the Commission finds that Auxier should monitor the quality of gas supplied to BOP immediately after initial service and for a period of 2 years thereafter, to ensure that the quality is adequate to serve the prison. Further, should the monitoring find that the gas quality is inadequate to the prison, Auxier must make the necessary modifications or additions to correct the inadequacies. In addition, a copy of this Order should be served upon BOP to ensure that it is fully aware that, on the facts demonstrated to the Commission, the gas to be supplied by Auxier, while meeting Kentucky's regulatory standards, may not meet the contract specifications.

Auxier supplied two estimates of the cost to build the pipeline. The original construction cost estimate, which was prepared by an independent engineering firm, was \$285,100. Auxier later provided a revised estimate of \$215,730, which was developed by Auxier itself. Neither estimate included the cost of the dryer. Auxier submitted a bid received for the dryer, which reflected an estimated capital cost of \$6,826. In the event that Auxier upgrades or replaces the proposed dryer, the actual cost of construction will increase accordingly.

Regardless of the construction cost estimate considered, the contract with the prison appears to cover Auxier's asset costs and the associated expenses for as long as the prison remains a sales customer of Auxier. However, the contract does allow the

prison to convert to transportation service after 1 year. If the prison does convert to transportation only, Auxier would experience a substantial annual operating loss, as its prison revenues would not cover the additional expenses associated with serving the prison. Additionally, the area around the pipeline has no development other than the prison. Therefore, Auxier cannot offset any losses incurred if the prison converts to transportation only with revenues from new customers. Auxier indicated that the likelihood of the prison converting to transportation service is not great, as another source gas is presently unavailable. If the prison does arrange for another supplier and converts to transportation service, Auxier should contact the Commission about other alternatives.

Auxier has proposed to finance this project by using internally generated funds to the extent that they are available. To the extent they are not available, Auxier will finance this long-term asset with a short-term line of credit of \$225,000 from the Community Trust Bank of Pikeville.

IT IS THEREFORE ORDERED that:

1. Auxier is granted a Certificate of Public Convenience and Necessity for the proposed construction project.
2. Auxier shall monitor the quality of the natural gas supplied to BOP immediately after initial service to the prison and for a period of 2 years thereafter. If the quality of gas is inadequate or declining, Auxier shall take immediate action to maintain the gas quality to the prison at an adequate level of service.
3. Auxier shall file its schedule of construction with the Commission 1 week prior to the actual start of construction.

4. Auxier shall provide the Commission copies of the “as-built” construction drawings of the pipeline and related appurtenances no later than 90 days after completion of construction.

5. Auxier shall file with the Commission the actual construction costs of the pipeline and related appurtenances no later than 90 days after completion of construction.

6. The “Natural Gas Utility Contract” between Auxier and BOP is approved.

7. A copy of this Order shall be served upon BOP to ensure that it is fully aware that, although the quality of gas to be delivered to it pursuant to the contract will meet regulatory standards, it may not meet the specifications of the contract itself.

Done at Frankfort, Kentucky, this 13th day of August, 2001.

By the Commission

ATTEST:


Executive Director