

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF ESSENTIAL)	
UTILITIES, INC., PNG COMPANIES LLC,)	
PEOPLES GAS KY LLC, AND DELTA)	CASE NO.
NATURAL GAS COMPANY, INC. FOR (1) A)	2020-00346
DECLARATORY ORDER AND (2) INCREASE)	
IN RATES FOR PEOPLES GAS KY LLC)	

ORDER

On October 27, 2020, pursuant to 807 KAR 5:026, Section 9 and 807 KAR 5:001, Section 19, Essential Utilities, Inc. (Essential), PNG Companies LLC (PNG), Peoples Gas KY LLC (Peoples KY), and Delta Natural Gas Company, Inc. (Delta), (collectively, Joint Applicants) submitted a joint application for (1) a declaratory order confirming that under KRS 278.020 Commission approval is not required for ownership of Peoples KY to be transferred to Delta, and (2) Commission approval of a rate increase for Peoples KY, setting the rates for Peoples KY to Delta’s current rate for farm-tap service. Joint Applicants assert that Commission approval of Peoples KY transfer to Delta is not required, because KRS 278.020(6)–(7) only applies to utilities as defined in KRS 278.010(3). Joint Applicants maintain that because the Commission has affirmed that Peoples KY is a farm-tap system,¹ and not a public utility² the Commission has no jurisdiction to review the transfer under KRS 278.020.

¹ A “farm-tap system” is a natural gas system in which retail gas service is provided to customers within one-half air mile of any producing well or gathering line, pursuant to KRS 278.485. Farm-tap systems are not considered utilities under KRS 278.010, because they do not furnish gas service to the public, but merely are obligated to offer gas service to customers in close proximity to the production or gathering facilities. The Commission has limited jurisdiction to regulate the retail rates of farm-tap systems.

By Order issued December 21, 2020, the Commission found that given the Commission's recent departure from prior decisions,³ an investigation was necessary to determine the applicability of KRS 278.020 to the proposed transaction. Pursuant to KRS 278.020(7), the Commission found good cause to continue Joint Applicants' application an additional 60 days. Joint Applicants have responded to one round of discovery. No one has sought intervention in this proceeding. Joint Applicants have not requested a hearing and this matter is ready for a decision based on the case record.

BACKGROUND

Essential, previously known as Aqua America, Inc. (Aqua America), a publicly held corporation organized under the laws of Pennsylvania, is the indirect owner of PNG, Delta, and Peoples KY.⁴ PNG, a limited liability company organized under the laws of Delaware, is the direct owner of Delta and Peoples KY.⁵ Delta is a Kentucky corporation providing gas service to 36,700 customers, including approximately 900 farm-tap customers, in 23 Kentucky counties.⁶ Peoples KY is a Kentucky limited liability company that provides farm-tap gas service to approximately 3,000 customers in eastern Kentucky.⁷

² Case No. 2018-00263, *Georgia Johnson v. Peoples Gas KY, LLC* (Ky. PSC Mar. 27, 2020).

³ Case No. 2020-00028, *Electronic Proposed Acquisition by Bluegrass Water Utility Operating Company, LLC of Wastewater System Facilities and Subsequent Tariffed Service to Users Presently Served by Those Facilities*, (Ky. PSC June 19, 2020), final Order at 16 in which the Commission announced its departure from precedent and indicated Commission approval for a public utility to acquire the system of a nonjurisdictional utility will henceforth be required.

⁴ Application at 1–2.

⁵ *Id.* at 2.

⁶ *Id.* at 2 and 5.

⁷ *Id.* at 4. Response to Staff's First Request (filed Jan. 29, 2021) Items 5, 7, 8, 9, 10. Peoples KY does not own any gathering lines or producing wells in Kentucky. Peoples KY sells gas to farm-tap

Subsequent to obtaining Commission approval in Case No. 2018-00369, Aqua America acquired indirect control over Delta's assets by acquiring 100 percent of LDC Funding LLC (LDC Funding) and LDC Funding's subsidiaries, including PNG, Peoples KY, and Delta.⁸ On February 3, 2020, Aqua America changed its name to Essential Utilities, Inc.⁹ Delta and Peoples KY remained wholly owned subsidiaries of PNG following the acquisition.¹⁰ Joint Applicants state they plan to dissolve Peoples KY as a standalone entity once the proposed transaction is consummated.¹¹

In Case No. 2018-00369, Aqua America made certain post-merger commitments associated with the transaction wherein, among other things, Aqua America committed that Delta and its ratepayers would not incur any additional costs, liabilities, or obligations in conjunction with the transaction, and would not bear costs associated with operating Aqua America's subsidiaries, including Peoples KY.¹² Joint Applicants state that the present rates of Peoples KY are deficient to the point that Peoples KY is unprofitable and losing over \$1.0 million per year on a pre-tax basis, with a retained deficit of \$4.4 million.¹³

customers along a gathering system formerly operated by the Kentucky West Virginia Gas Company. Peoples KY's gas supplier is Diversified Southern Production.

⁸ Case No. 2018-00369, *Electronic Joint Application of Aqua America, Inc., SteelRiver Infrastructure Fund North America LP, SteelRiver LDC Investments LP, LDC Parent LLC, PNG Companies LLC, Peoples Gas KY LLC, and Delta Natural Gas Company, Inc. for Approval of an Acquisition of Ownership and Control of PNG Companies LLC and Delta Natural Gas Company, Inc.* (Ky. PSC Mar. 13, 2019).

⁹ Application at 2.

¹⁰ Response to Commission Staff's First Request (Response to Staff's First Request), (filed Jan. 29, 2021), Attachment to Item 13(b), Organizational Chart.

¹¹ Application at 6.

¹² Case No. 2018-00369, *Electronic Joint Application of Aqua America, Inc.* (Ky. PSC Mar. 13, 2019), Order at 6. Application at 5-6.

¹³ Application at 3-4 and 7.

For this reason, Joint Applicants condition the proposed transaction on the Commission's approval of a rate increase for Peoples KY's customers to bring these rates up to the rates currently being charged Delta's farm-tap customers. The Commission finds that a review of Joint Applicants' proposed transaction is necessary to ensure continued compliance with the commitments made to Delta and its ratepayers in Case. No. 2018-00369.

DISCUSSION

Joint Applicants state that since the acquisition, they have been analyzing their respective structures and operations and have identified opportunities with respect to Peoples KY and Delta. Joint Applicants state that Peoples KY employees in Pennsylvania provide current day-to-day oversight of Peoples KY's farm-tap operations. Joint Applicants note that Delta operates a gas system in Kentucky that already provides retail and farm-tap service, and that shifting the ownership and control of Peoples KY to Delta will provide local Kentucky-based leadership to Peoples KY.¹⁴ Joint Applicants state that Delta and Peoples KY service territories adjoin, and a transfer of Peoples KY day-to-day operations to Delta will permit a more efficient operation of Peoples KY's system than at present.¹⁵

Joint Applicants explain that Peoples KY's only office is in Pikeville, Kentucky, and that Delta has an office in Manchester, Kentucky from which it deploys field technicians.¹⁶ Joint Applicants further explain that Delta's Manchester office is located near where both

¹⁴ *Id.* at 3.

¹⁵ *Id.* at 5–6.

¹⁶ *Id.* at 6.

Delta and Peoples KY already have farm-tap customers and that having technicians located more broadly throughout Peoples KY's system will result in additional operating enhancements. Joint Applicants state that Delta can assist and further train Peoples KY's technicians in automated meter reading, calibration, and collection methods.¹⁷ Joint Applicants state that Delta is transitioning to the SAP Customer Relationship and Billing System in 2021, and Peoples KY has already converted to this system. Joint Applicants maintain that the merger of Delta and Peoples KY will facilitate a reduction in the amount of manual work to be done in each billing cycle because Delta can integrate the Peoples KY collection data into Delta's billing system.¹⁸

The Commission is reviewing the proposed transaction for the purpose of confirming that neither Delta nor its ratepayers will subsidize Peoples KY's operations or will otherwise be financially harmed by the proposed transfer of Peoples KY to Delta. However, if Peoples KY were a public utility and not a farm-tap system, the Commission would review the proposed transaction pursuant to KRS 278.020(6) and KRS 278.020(7). The Commission includes a discussion of the requirements of KRS 278.020(6) solely to demonstrate that if this transaction were subject to that statutory provision, the requirements have been met.

KRS 278.020(6) provides that:

No person shall acquire or transfer ownership of, or control, or the right to control, any utility under the jurisdiction of the commission by sale of assets, transfer of stock, or otherwise, or abandon the same, without prior approval by the commission. The Commission shall grant its approval if the person acquiring the utility has the financial, technical, and managerial abilities to provide reasonable service.

¹⁷ *Id.*

¹⁸ *Id.*

Delta is currently operating a gas utility and providing farm-tap service to 36,700 customers, including over 900 farm-tap customers. This is sufficient evidence that Delta has the financial, technical, and managerial abilities to operate a gas utility and a farm-tap system. Additionally, according to its most recently filed annual report Delta has a net utility plant of \$147,558,610,¹⁹ and retained earnings of \$5,152,635.²⁰ For the calendar year ended December 31, 2019, Delta reported total gas operating revenues of \$47,621,235 and net income of \$7,133,139.²¹

Given the case record and being otherwise sufficiently advised, the Commission finds that Delta has the financial, technical, and managerial abilities to provide reasonable farm-tap service and that transfer of Peoples KY to Delta will not negatively affect Delta's ability to provide natural gas service. The Commission further finds that the transfer of ownership of Peoples KY to Delta should be approved.

In support of their claim that Delta will not subsidize People's KY's operations following the proposed transfer, Joint Applicants state that Peoples KY's operational costs are not expected to increase as a result of the transfer, and there will be no system implementation costs in merging the operations of Delta and Peoples KY.²² Given Joint Applicants claim that Peoples KY's rates are inadequate, and to further ensure Delta does not suffer financial harm, pursuant to 804 KAR 5:026, Section 9, Joint Applicants also seek to increase People KY's rates by applying the rate paid by Delta's farm-tap

¹⁹ *Annual Report of Delta Natural Gas Company, Inc. for the Year Ended December 31, 2019*, at 14.

²⁰ *Id.* at 17.

²¹ *Id.* at 19 and 22.

²² Application at 6.

customers to Peoples KY's customers. Joint Applicants propose not assessing Delta's Gas Cost Adjustment Clause (GCR) and Pipe Replacement Program tariffed charges to Peoples KY's customers because at least initially, this portion of the system will be operated in a physically discrete manner.²³ Joint Applicants propose continuing to apply Peoples KY's GCR to Peoples KY's customers and incorporating this into Delta's tariff.²⁴

Joint Applicants state that the proposed rate change will increase the average bill for a Peoples KY's customer from \$37.77 to \$59.93.²⁵ This is a 59 percent increase in the average Peoples KY's customer's bill.²⁶ The rates charged to farm-tap customers must be approved by the Commission. Commission Regulation 807 KAR 5:026, Section 9, allows a farm-tap operator to request an adjustment in retail rates through a proposed tariff 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 filed²⁷ 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. If the proposed percentage increase in rates exceeds the percentage change in the price index but the proposed rate remains below the highest prevailing gas rate approved by the Commission, the gas company must submit its proposed tariff and cost data that supports the proposed increase.

²³ *Id.* at 7.

²⁴ *Id.*

²⁵ *Id.*

²⁶ Application, Exhibit 5.

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

The percentage change in the price index during the 12-month period ending September 30, 2020, is 2.47 percent, which is lower than the proposed 59 percent increase in rates.²⁸ However, the proposed rates are below the highest prevailing gas rates approved by the Commission, which are those currently being charged by G.S. Knox, Interstate Natural Gas, and Troublesome Creek.²⁹ Because Peoples KY does not meet the first test cited in 807 KAR 5:026, Section 9(a), but does meet the second, 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.³⁰ Peoples KY submitted the required cost data supporting the proposed increase.³¹

Having considered the evidence of record and being otherwise sufficiently advised, the Commission finds the rates in the Appendix to this Order meet the requirements of 807 KAR 5:026, Section 9, should be approved, and should be effective upon the date of consummation of the transfer of ownership of Peoples KY to Delta.

The Commission notes that Delta's last general rate increase was in October 2010,³² and that Delta has not identified a date when it will file its next general rate case.³³ The Commission further notes that (1) Delta's tariff does not provide a separate rate schedule for farm-tap customers; (2) Delta has not considered establishing a separate

²⁸ $186.6 \text{ (CPI September 30, 2020)} - 182.1 \text{ (CPI October 1, 2019)} = 4.5 \div 182.1 \text{ (CPI October 1, 2019)} = 2.47\%$.

²⁹ Application at 8.

³⁰ 807 KAR 5:026, Section 9(b).

³¹ Response to Staff's First Request (filed Jan. 29, 2021), Items 23(a) and 23(b) including Attachment 23(a) and Attachment 23(b).

³² Case No. 2010-00116, *Application of Delta Natural Gas Company, Inc. for an Adjustment of Rates*. (Ky. PSC Oct. 21, 2010).

³³ Response to Staff's First Request (filed Jan. 29, 2021), Item 15(c).

rate schedule for its farm-tap customers;³⁴ and (3) when Delta was ordered to establish a separate rate schedule for farm-tap customers,³⁵ it cited its limited number of farm-tap customers and claimed the requirement presented complications that outweighed the benefit of establishing a separate rate for so few customers. The Commission subsequently relieved Delta of that requirement.³⁶ However, the merger of Delta and Peoples KY significantly increases the number of farm-tap customers being served by Delta and being charged Delta's residential customer rate.

The Commission's review of the proposed increase to Peoples KY's farm-tap rates pursuant to 807 KAR 5:026, Section 9, the regulation under which this application was filed, did not address the issue of whether Delta's farm-tap rates are fair, just and reasonable given that the merger will more than triple the number of farm-tap customers on Delta's system, and that market conditions have changed considerably since 2010. Having considered the evidence of record and being otherwise sufficiently advised, the Commission finds that an investigation into the reasonableness of Delta's farm-tap rates is necessary.

IT IS THEREFORE ORDERED that:

1. The proposed transfer of ownership of Peoples KY to Delta is approved.
2. Within five days of consummation of the transfer, Delta shall file a written notice settling forth the date of the transfer and referencing this case number. The notice shall be retained in the post-case correspondence file.

³⁴ *Id.* at Item 4.

³⁵ Case No. 2000-00468, *Charles B. Gregory v. Columbia Natural Resources and Delta Natural Gas Company, Inc.* (Ky. PSC Nov. 28, 2001).

³⁶ Case No. 2000-00468, (Ky. PSC Feb. 25, 2002), final Order.

3. The rates set forth in the Appendix to this Order are approved.
4. The effective date of the rates set forth in the Appendix shall be the date the transfer of ownership of Peoples KY to Delta is consummated.
5. Within ten days of the transfer of Peoples KY to Delta, Peoples KY shall file revised tariff sheets with the Commission, using the Commission's electronic Tariff Filing System, containing the rates set forth in the Appendix to this Order.
6. The Commission shall initiate a separate proceeding in which to investigate the reasonableness of Delta's farm-tap rates.
7. This case is closed and removed from the Commission's docket.

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By the Commission



ATTEST:



Linda C. Adwell
Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2020-00346 DATED FEB 22 2021

The following rates and charges are prescribed for the customers in the area served by Peoples Gas KY LLC. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the authority of the Commission prior to the effective date of this Order.

	<u>Base Rate</u>
Customer Charge	\$21.00
All Mcf	\$ 4.3185

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