IN THE SUPERIOR COURT OF THE STATE OF DELAWARE
IN AND FOR KENT COUNTY

Chesapeake Utilities Corporation,	:	
	:	C.A. No: K10A-06-008 (RBY)
Appellee/Cross-Appellant,	:	
	:	
v.	:	
	:	
G. Arthur Padmore, Public Advocate,	:	
	:	
Appellant/Cross-Appellee,	:	
	:	
v.	:	
	:	
The Delaware Public Service Commission,	:	
	:	
Appellee.	:	

Submitted: March 14, 2011
Decided: June 13, 2011

Upon Consideration of
Appeal from the
Delaware Public Service Commission
AFFIRMED

OPINION AND ORDER

William A. Denman, Esq., Parkowski, Guerke & Swayze, P.A., Dover, Delaware for Chesapeake Utilities Corporation.

Kent Walker, Esq., Department of Justice, Wilmington, Delaware for G. Arthur Padmore, Public Advocate.

Regina A. Iorii, Esq., Department of Justice, Wilmington, Delaware for the Delaware Public Service Commission.

Young, J.

Summary

______This appeal arises out of an annual Gas Service Sales Rates ("GSR") application filed by appellant Chesapeake Utilities Corporation Delaware Division ("Chesapeake") with the Delaware Public Service Commission ("Commission").The Public Advocate, Arthur Padmore ("Public Advocate") intervened.[1] The case went before a Hearing Examiner, and then before the Commission. Chesapeake and the Public Advocate filed this appeal and cross appeal from the Commission's final Order No. 7778 pursuant to 29 *Del. C.* § 10142.

______Because the actions of the Commission do not infringe upon federal authority, and because substantial evidence exists in the record to support the Commission's findings, the decision of the Commission is **AFFIRMED**.

Background on the Natural Gas Act and Industry

The Natural Gas Act ("NGA") regulates the natural gas industry throughout the nation. The Federal Energy Regulatory Commission ("FERC")is the administrative agency that issues regulations, orders, and guidance on how the natural gas industry is to be regulated. The FERC issued Order Nos. 436 and 636, instituting a uniform national "capacity release" program, exercising its power under NGA section 5 to conform pipelines' existing capacity agreements.

Capacity release arrangements involve the releasing shipper's decision to sell excess capacity on the pipeline. Under capacity release, each interstate pipeline is required to establish and administer an electronic bulletin board (a computer through which putative releasing and replacement shippers may communicate). Holders of

[1] During the course of this appeal, Mr. Arthur Padmore retired and Petitioner Joseph R. Biden, III was substituted until a successor is appointed as Public Advocate.

the excess firm capacity rights may post their available capacity on the board, and then establish nondiscriminatory conditions for the sale. The pipeline must then sell the capacity to the highest bidder. The price for released capacity may not exceed the maximum rate set by FERC for the capacity.

_____After the replacement shipper has been chosen, the pipeline enters into a contract with it for firm capacity rights. The pipeline may elect to excuse completely the releasing shipper's obligation to pay the reservation fee and the related costs. Otherwise, the releasing shipper is credited for those costs unless the replacement shipper defaults. The releasing shipper is not liable for costs associated with the replacement shipper's transportation of the natural gas on the pipeline.

Procedural History

On September 2, 2008, Chesapeake filed with the Commission its annual application seeking approval to decrease its GSR rates effective November 1, 2008. The Delaware Public Advocate intervened. Pursuant to a settlement subsequently approved by the Commission, the proposed decrease in rates was approved. The settlement, submitted on June 11, 2009, resolved all issues except whether Chesapeake was releasing pipeline capacity to its affiliate Peninsula Energy Service Company ("PESCO") on terms and conditions consistent with Commission rules and regulations and with applicable law.

The Commission approved the settlement agreement, but deferred the remaining issue to a "Phase II". The Phase II proceeding was necessary to address whether Chesapeake must follow "asymmetric pricing" when and if Chesapeake releases pipeline capacity to PESCO. The concept of "asymmetric pricing" provides that, if a utility transfers an asset to an affiliate, or performs a service for the affiliate, the utility must charge the affiliate a price equal to the utility's "cost" or "market value," whichever is higher.

The issue was assigned to a Hearing Examiner for Phase II of the case. The parties submitted pre-filed testimony which, in part, was admitted into evidence. On September 2, 2009, the Hearing Examiner held a hearing. On January 7, 2010, the Hearing Examiner issued proposed findings and recommendations, concluding that asymmetrical pricing is required for capacity releases to PESCO.

______The Hearing Examiner determined that Chesapeake could release capacity to PESCO at any rate it chose; but, if Chesapeake released capacity at a rate less than the "maximum rate," it must credit the GSR with the difference between the applicable FERC "maximum rate" and the actual release rate paid by PESCO. The "maximum rate" is the cost Chesapeake pays for the capacity from the interstate pipeline. It was recommended that the credit be calculated back to January 2008, when Chesapeake first began releasing capacity to PESCO. Chesapeake filed exceptions to the Hearing Examiner's findings and recommendations before the Commission.

On February 18, 2010, the Commission met to hear argument and deliberate. Oral argument was held before the Commission on two separate occasions. On March 30, 2010, the parties addressed certain issues in supplemental filings, and the Commission heard additional argument. On May 18, 2010, after deliberations the Commission issued Order No. 7778. Chesapeake and the Public Advocate petitioned for reconsideration which the Commission denied on July 6, 2010. This appeal followed.

<u>The Commission's Findings of Fact</u>

The following findings of fact were adopted from the Delaware Public Service Commission's Order No. 7778.

> Chesapeake's Delaware Division provides service to some 38,300 customers located in southern New Castle, Kent and Sussex counties, approximately 91% of which are residential. The Delaware Division is connected to only one interstate natural gas pipeline, its affiliate Eastern Shore Natural Gas Company ("ESNG"); there are no other interstate pipelines in the immediate vicinity through which Chesapeake can transport natural gas. The Delaware Division has transportation entitlements with ESNG which, in turn, are supported by upstream transportation entitlements and storage agreements. Hence, all gas delivered to Delaware Division customers flows through ESNG's pipelines. ESNG is regulated by the Federal Energy Regulatory Commission ("FERC").
>
> The Company purchases firm, long-term pipeline capacity from ESNG at the maximum FERC- approved rates of approximately 30 cents per dekatherm ("DTH") for Delaware Zone 1 and approximately 56 cents per Dth for Delaware Zone 2 to serve its firm customers on a design day. The Company charges the maximum FERC-approved rates of 30 cents per Dth for Delaware Zone 2 to serve its firm customers on a design day. The Company charges the maximum FERC-approved rates of 30 cents per Dth for pipeline capacity releases to firm Delaware Zone 1 customers and 59 cents per Dth for pipeline capacity releases to firm Delaware Zone 2 customers.
>
> In Docket No. 00-523, this Commission approved a settlement that, among other things, established a Cost Accounting Manual and a Code of Conduct for Chesapeake. The following language of the Settlement Agreement in that case sets forth pricing principles to be applied to certain types of affiliate transactions in the future:
>
>> Pricing Principles. The Settling Parties agree that subject to the provisions set forth below, for transfer of assets between Regulated

> Activities ("Chesapeake")and Non-Regulated Activities, ("Affiliate") asymmetric pricing principles (i.e. for transfers from Chesapeake to the Affiliate, the higher of fully allocated cost or market price; for transfers from the Affiliate to Chesapeake, the lower of fully allocated cost or market price) shall apply. Asymmetric pricing principles shall also apply to the provision of services, exclusive of shared services or common support services, provided however that if the market price of such service is not reasonably ascertainable, fully allocated costs will be used.

Additionally, the settlement contained a provision that, if Chesapeake decided to own and/or operate a marketing affiliate, or if its non-utility operations were selling natural gas in Delaware, the following Code of Conduct provisions would apply:

> The following Standard of Conduct shall apply to transactions between Chesapeake Utilities Corporation – Delaware Division, Non-Regulated Activities, and Third Parties.
>
> 3. Chesapeake Utilities Corporation – Delaware Division or any Non-Regulated Activities may not represent that the utility will give any preference to a customer or others in the use of Natural Gas Distribution Utility Services as a result of that customer or others dealing with the Non-Regulated Activities.
>
> 4. Chesapeake Utilities Corporation – Delaware Division may not give any

> preference to its Non-Regulated Activities or customers of its Non-regulated Activities in the provision of Natural Gas Distribution Utility Services.

Prior to the Company's last base rate case (Docket No. 07-186), the Company had provided interruptible sales service to eleven off-system sales ("OSS") customers. In Docket Nos. 07-186 and 07-246F (the GSR case immediately preceding the present docket), Chesapeake stated that it intended to stop making off-system sales. Chesapeake subsequently transferred its OSS customers to its affiliate, Peninsula Energy Service Company ("PESCO"), and began to release pipeline capacity to PESCO to enable PESCO to serve these customers.

Prior to Chesapeake's announcement that it intended to cease making off-system sales, margins from the Company's off-system sales were shared between shareholders and ratepayers. To alleviate concerns over the regulatory impact of Chesapeake's exit from its merchant function and the anticipated transfer of its OSS customers, the Company committed to credit the GSR for 100% of the revenues it received for any pipeline capacity released to serve the former customers. The settling parties intended the credit to equal what would have been credited to Chesapeake's firm customers through the margin sharing mechanism had these OSS customers remained the Company's customers. This was consistent with the existing requirement that the Company credit 100% of ESNG pipeline capacity release revenues to the GSR since ratepayers pay for 100% of the cost of the pipeline capacity through the GSR. The settlement in PSC Docket 07-246F did not require that the release rate be equal to the higher of "cost" or "market." We approved the settlement in PSC Docket 07-246F in Order. 7450 dated October 7, 2008.

In Phase I of this docket, the Company disclosed that it was charging PESCO 17 cents per Dth for the pipeline capacity it releases to PESCO and with which capacity PESCO supplies Chesapeake's former OSS customers. In designing the rate, the Company divided $160,000 (the historical five-year average annual margins previously credited to firm customers when the Company was making OSS) by the number of Dths that the Company estimated PESCO would need to serve the OSS customers, and arrived at a rate of $0.17 per Dth. In Phase II of this docket, the Company presented the testimony of Jennifer Clausius that, in Docket 07-246F, the Company informed the parties that the historical five-year average of OSS margins credited to the firm customers totaled approximately $160,000 per year that the Company would release capacity at a rate that would equate to a credit for capacity release revenue approximating the 5 year average annual margin share under the discontinued OSS program.

FERC regulates the release of pipeline capacity on interstate pipelines. With respect to the $0.17 per Dth capacity release rate designed by the Company for capacity releases to PESCO, as allowed by FERC's capacity release rules, the Company entered into capacity release agreements with PESCO as a redesignated replacement shipper. Under FERC rules, the Company was required to post the $0.17 per Dth proposed rate on an electronic bulletin board, and provide other interested parties with the opportunity to submit competing bids. However, PESCO would have the right to receive all of the capacity, provided PESCO met the highest competing bid.

The Company credits all capacity release revenues to its Delaware firm customers through a reduction in the cost paid by the Company to ESNG. PESCO does not pay any sums to Chesapeake. In accordance with ESNG's FERC-approved tariff rules, PESCO pays ESNG directly for the capacity. For the twelve-month period ending December, 2008, the actual GSR credit for capacity released to PESCO was $198,880. For the five-month period ending May, 2009, the GSR credit was $189,343.[2]

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[2] *In the Matter of the application of Chesapeake Utilities Corp.*, 281 P.U.R. 4th 119, *1 (internal citations omitted).

The Commission's Conclusions of Law

In its order, the Commission acknowledged that this was a very difficult matter to resolve, since there were compelling arguments on both sides. The Commission considered the entire record and the arguments of the parties. Ultimately, the Commission found the following: (1) the FERC's exercise of jurisdiction over capacity release transactions does not preclude the Commission from determining what effect those capacity transactions will have on Delaware retail rates; (2) the Hearing Examiner's Report was accepted and modified; (3) from the date of the Order, the asymmetrical pricing principles approved in the settlement shall be applied[3]; (4) Chesapeake shall not be required to credit the GSR with the difference between the maximum FERC-approved rate and the amount it received for capacity release transactions between it and its affiliate PESCO from January 1, 2008 to the present; (5) Chesapeake was instructed to file an application to open a new docket in which the Commission will consider whether to apply asymmetrical pricing principles to capacity release transactions between a regulated utility and a non-regulated affiliate in light of the FERC rules governing such transactions.

_____The Commission determined that it could address the matter without running afoul of the FERC's jurisdiction in the area of capacity release transactions. In concluding that the FERC's exercise of jurisdiction over capacity release transactions does not preclude the Commission from determining the effect on Delaware retail

[3] The settlement of the parties was approved in Docket No. 00-523. The Commission held that should the Company (Chesapeake) release capacity to any affiliated company at less than the applicable FERC-approved maximum price for the applicable zone, not only will the amount the Company actually received from the transaction be credited to the GSR but also the difference between the maximum FERC-approved applicable zone rate and the amount received by the Company from the transaction shall also be credited to the GSR.

rates, the Commission contrasted the case at hand with *United Distribution Companies v. Federal Energy Regulatory Commission.*[4]

In the *United Distribution* case, the D.C. Circuit Court of Appeals considered the question of the extent of the FERC's jurisdiction over capacity release transactions, not how capacity release transactions between a regulated utility and its non-regulated marketing affiliate will be treated for retail rate making purposes. The Commission also considered *Kentucky West Virginia Gas Company v. Pennsylvania PUC*[5], a Third Circuit Case, which held that FERC has no jurisdiction over retail rates in *Kentucky West Virginia*.

_____In addition, the Commission found that asymmetrical pricing applies to Chesapeake's transactions with PESCO.[6] This has been the rule of law since 2001. It is applicable to capacity release transactions between Chesapeake and its non-regulated marketing affiliate, PESCO. Further, the Commission found that competition is not thwarted; that the Commission's order does not circumvent the FERC's posting and bidding rules; and that Chesapeake can still post the capacity for bid, permitting PESCO and others to bid.

Finally, the Commission found that the parties' settlement agreement (Order

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[4] 88 F.3d 1105 (D.C. Cir. 1996) (addressing the buy-sell program that allowed end users to skirt the posting and bidding requirements of FERC's capacity release rules was invalidated by the Court because it was in direct conflict with the FERC's jurisdiction).

[5] 837 F.2d 600 (3d Cir. 1988) (holding that a state commission is permitted to determine the justness and reasonableness of gas purchases from its subsidiary in exercising authority over intrastate utility rates).

[6] The concept of "asymmetric pricing" provides that if a utility transfers an asset to an affiliate, or performs a service for the affiliate, the utility must charge the affiliate a price equal to the utility's "cost" or "market value," whichever is higher.

No. 7450 in Docket No. 07-246F) does not abrogate the requirement of asymmetrical pricing for affiliated transactions. Chesapeake, in releasing capacity, was transferring an asset and a service to PESCO. As such, PESCO pays value for the asset, benefitting Chesapeake in the form of a reduction in the amount of ESNG bills for the purchased capacity.

Standard of Review

_____On appeal from an administrative agency decision, the reviewing court must determine whether the agency ruling is supported by substantial evidence and free from legal error.[7] "Substantial evidence is such relevant evidence as a reasonable mind might accept as adequate to support a conclusion. It must be more than a scintilla, but may be less than a preponderance of the evidence."[8] Absent an abuse of discretion, the agency's decision must be affirmed.[9] "When the issue is one of agency interpretation of statutory law, and application of that law to undisputed facts, this Court's review of the agency's decision is plenary, and it is not bound by the agency's conclusion."[10] This Court nevertheless, will give substantial weight to an agency's interpretation of a statute that agency is empowered to enforce.[11]

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[7] *Public Water Supply Co. v. DiPasquale,* 735 A.2d 378, 383 (Del. 1999) (citing *State, Dept. Of Labor v. Medical Placement Services, Inc.*, 467 A.2d 454 (Del. 1983).

[8] *Olney v. Cooch*, 325 A.2d 610, 614 (Del. Supr. 1981); *Price v. State of Delaware Board of Trustees*, 2010 Del. Super. LEXIS 120 (Mar. 22, 2010).

[9] *Id.*

[10] *DiPasquale*, 735 A.2d at 381.

[11] *Id.*

Issues Presented

There are two principle issues presented on appeal to this Court. The first is whether the Commission is preempted by Federal law, from exercising its jurisdiction over the rates charged by Chesapeake in its transfer of an asset with value to an unregulated affiliate for less than what Chesapeake paid. In conjunction with that is whether the Commission properly determined that it would not be appropriate to order Chesapeake to credit the capacity release. The second is whether the rate payers of Delaware were unduly prejudiced by the Commission's findings.

Contentions of the Parties

A. Chesapeake Utilities Corporation

Chesapeake contends that the Delaware Public Service Commission is preempted by the FERC pipeline capacity release regulations from penalizing the company for releasing capacity to an affiliate at less than maximum rates. Chesapeake argues that the FERC's capacity release rules allow firm pipeline capacity holders, such as Chesapeake, to release their capacity. Chesapeake contends that, to the extent it engages in capacity releases, it is subject to FERC jurisdiction, even though in other matters it is subject to the jurisdiction of the Delaware Commission.

Chesapeake contends that the Commission's order that Chesapeake must either apply asymmetrical pricing principles by charging only the maximum rate in its capacity releases to PESCO, or pay a penalty if it releases capacity to PESCO at a lower rate, effectively thwarts the competitive bidding process set forth in the FERC's rules. Chesapeake argues that it is penalized for releasing capacity to its affiliate at a rate determined under the transparent bidding rules issued by the FERC. Imputed on Chesapeake is a credit from the pipeline for temporary capacity releases to PESCO, which is much higher than the amount PESCO pays to the pipeline for the capacity from Chesapeake. This, it is argued, essentially discourages capacity releases, discriminates against PESCO in relation to other bidders, and stands as an obstacle to the FERC's capacity release rules.

B. The Public Advocate

In addressing Chesapeake's objections on appeal, the Public Advocate contends that Chesapeake, in essence, is attempting to launder its capacity release transactions through the FERC's bidding program. That self dealing, the Public Advocate asserts, has a pernicious impact on Delaware ratepayers. The Public Advocate contends that PESCO is not an independent entity from Chesapeake. Hence, the Public Advocate asserts the following arguments on appeal: (1) Order No. 7778 unlawfully alters Chesapeake's rates retroactively; (2) Order No. 7778 alters an existing rate without substantial evidence or a finding that the rates are just and reasonable; (3) the record doesn't support the Commission's finding that ratepayers are not prejudiced by applying asymmetric pricing; (4) Chesapeake has not met its burden of establishing that its GSR rates were just and reasonable; and (5) the Commission's "sanctions" on Chesapeake were arbitrary and an abuse of discretion.

C. The Delaware Public Service Commission

The Commission contends that it is not preempted from applying its affiliated transactions rules to Chesapeake's transfers of pipeline capacity to PESCO. In response to Chesapeake's arguments on appeal, the Commission contends that it has not regulated capacity releases. Instead, the Commission states, it was regulating the transfer of an asset by Chesapeake to PESCO.

In addressing the Public Advocate's arguments on appeal, the Commission contends that it correctly determined that there was insufficient evidence to find that ratepayers were "unfairly prejudiced," finding, to the contrary, that the equities support prospective application of asymmetrical pricing. Furthermore, the Commission claims that substantial evidence below exists to support the Commission's decision and that the altered rates were just and reasonable.

DISCUSSION

A. Federal Preemption Issue:

First, we look to whether or not the Commission's order is preempted by the Natural Gas Act and the jurisdiction of the FERC. The United States Constitution provides that the laws of the federal government "shall be the supreme Law of the land; ...any Thing in the Constitution or Laws of any State to the Contrary notwithstanding."[12] This principle of Supremacy is implemented through the doctrine of federal preemption. Thus, state and local laws are stripped of their effect when they conflict with a federal regulation issued by administrative agencies. The parties here do not dispute that the federal agency, the FERC, has exclusive jurisdiction over firm capacity releases.

The Natural Gas Act states in relevant part:

> (b) The provisions of this chapter shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural

[12] U.S. CONST. Art. VI.

> gas or to the facilities used for such distribution or to the production or gathering of natural gas.[13]

The Natural Gas Act grants the FERC exclusive authority to regulate the transportation of natural gas in interstate commerce. This includes primary jurisdiction over interstate pipeline transportation service agreements. Included within interstate pipeline transportation are customers (shippers) and the shippers' temporary or permanent assignment or release of their capacity rights under such pipeline service agreements. The parties are not disputing that the FERC has exclusive jurisdiction over capacity releases. The dispute of the parties is whether the Commission is attempting to regulate indirectly the sale in interstate commerce of natural gas.

Relying heavily on the *United Distribution* and the *Georgia Public Service Commission* cases, Chesapeake contends that the Commission's decision is an attempt to regulate Chesapeake's activities and ability to release capacity, which are subject to exclusive federal regulation under the FERC. The Commission does not dispute the exclusive jurisdiction of the FERC to regulate the area of capacity releases. Chesapeake does not dispute the Commission's jurisdiction to regulate Delaware retail rates.

In the *United Distribution* case, the Court of Appeals for the District of Columbia addressed a state buy-sell program, reviewing the extent of the FERC's jurisdictional scope over capacity release transactions.[14] The Court discussed at great

[13] 15 U.S.C. § 717(b).

[14] 88 F.3d 1105 (D.C. Cir. 1996), cert. denied sub nom.

length capacity releases and the interdisciplinary relationships which exists between the agency, companies, the pipelines and states.[15] The Court held that the FERC has exclusive jurisdiction in regulating and setting the procedures and pricing schemes for firm capacity releases.[16]

In *Georgia Public Service Commission*, the Georgia Public Service Commission filed a Petition for Declaratory Order. The order requested that the FERC address the issue of whether the FERC would preempt the Georgia Commission. The Georgia Commission adopted a plan that provided for the permanent assignment of the interstate capacity assets currently held by Atlanta Gas Light Company. The plan assigned the capacity assets to certificated natural gas marketers, and placed conditions upon that assignment of the interstate capacity assets. The attempt in that case was to implement a retail unbundling program mandated by the Georgia legislature.

The FERC found that the Georgia Commission was preempted. However, it recognized room for states to exercise authority involving pipeline capacity releases. The FERC stated:

> The GPSC has authority to mandate how much interstate pipeline capacity Atlanta (the LDC) or a Georgia marketer should hold. Thus, for example, it can order Atlanta to obtain more capacity if needed, or to relinquish unneeded capacity so that Georgia consumers do not have to pay for such unneeded capacity. The same holds true for the GPSC's regulation of Georgia marketers. However, the GPSC's regulation of access to, use of and recall or reversion of such interstate pipeline capacity appears to intrude on the Commission's exclusive jurisdiction

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[15] *Id.*

[16] *Id.*

> over such matters. The GPSC, through its regulation of Atlanta and Georgia marketers, appears to be essentially regulating who interstate pipelines may serve, where such service may be provided, and for what levels of service.[17]

Unlike the issue in *Georgia Public Service*, the crux of Order 7778 is not Chesapeake's capacity releases to PESCO, but the transfer of an asset to an unregulated affiliate for less than what Chesapeake paid for it. As the Commission found below, Order 7778 is not regulating access to, use of, or recall or reversion of interstate pipeline capacity. It is not precluding Chesapeake from selling its excess capacity. The FERC, as stated above, acknowledged that state commissions have authority to obtain more capacity or to relinquish it in order to prevent the state consumers from having to pay for unneeded capacity.

Under the Natural Gas Act guidelines, the FERC has jurisdiction over the sale of the excess capacity. Here, though, the Commission exercised jurisdiction over the transfer of assets or services between a regulated public utility and an unregulated affiliate for which Delaware ratepayers would be affected. The central element of the Commission's order was not capacity releases to PESCO. Rather the fact that Chesapeake was transferring an asset that has significant value to an unregulated affiliate, PESCO, was the question. Chesapeake paid significantly less for the asset that it was transferring to its affiliate and subsidiary, PESCO. Pursuant to 26 *Del. C.* § 301, the Commission has authority to set Chesapeake's rates. As the Commission notes in its brief, if this case did not involve an affiliate, the case simply would not exist.

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[17] 2004 WL 821537 (FERC Apr. 15, 2004).

The Commission's findings do not run afoul of either *United* or *Georgia Public Service*. The Commission found that Chesapeake is transferring an asset that has significant value to an unregulated affiliate for far less than Chesapeake paid for it. This is within the Commission's jurisdiction. The transfer of the asset in this case consists of the transfer of capacity releases, which consequently raises preemption questions due to the jurisdiction of the FERC.

This case does not infringe upon the jurisdiction of the FERC. Thus, the Commission is not preempted. However, even if capacity releases were the central issue (and not the transfer of an asset, being the capacity releases), the FERC has acknowledged that there is room for states to exercise their authority. As noted, in *Georgia Public Service*, the FERC discussed that there may be situations involving pipeline capacity releases, such as this case, where states would have jurisdiction over certain matters.

The *United* case is inapposite, because there the Commission was attempting to regulate the actual practice of capacity releases. Hence, there the Court held that a company's capacity releases are within the exclusive jurisdiction of the FERC. The Commission appropriately maintains that this case is not one which dealt with capacity releases. Instead, this is a retail rate case, over which the Commission has jurisdiction.

B. Unduly Prejudicial

To summarize: the Commission found that asymmetrical pricing is applicable to the capacity release transactions between Chesapeake and PESCO. The Commission also determined that to require Chesapeake to credit the GSR with the difference between the maximum rate and what PESCO paid for the capacity going back to January 2008 would not constitute retroactive rate making, prohibited by 26 *Del. C.* § 311. However, the Commission concluded that Chesapeake will not be required to credit the GSR with the difference between the maximum FERC-approved rate and the amount received for capacity release transactions between it and its affiliate PESCO from January 1, 2008 to the present May 18, 2010. The Commission explained its reasoning as follows:

> We do not believe that there is sufficient evidence on the record to establish that ratepayers were unfairly prejudiced. Furthermore, under the unusual circumstances of this case, we do not believe it would be equitable to require the Company to credit the GSR for that difference.

The Public Advocate contends that since the Commission determined that asymmetrical pricing principles were in effect at the time Chesapeake released capacity to PESCO, Chesapeake is required to credit its Delaware ratepayers with the difference between its cost of capacity and the credit it received for the release of that capacity to its affiliate PESCO.

Pursuant to 26 *Del. C.* § 311:

> If, after hearing, the Commission finds any existing or proposed rate unjust, unreasonable or unjustly discriminatory, or in any wise in violation of law, the Commission shall determine the just and reasonable rate to be charged or applied by the utility for the service in question, and shall fix the same by order to be served upon the utility; and such rate shall thereafter be observed until changed, as provided in this chapter. In determining the just and reasonable rate to be charged, the Commission shall consider the revenue needs of the utility, its past and projected rates of return on its rate base, or, when appropriate, its operating ratio.[18]

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[18] 26 *Del. C.* § 311

The Delaware Supreme Court in *Public Service Commission v. Diamond State Telephone Company*, held that the Commission's statutory authority to determine just and reasonable rates is prospective only.[19] A pervasive and fundamental rule underlying the utility rate-making process is that "rates are exclusively prospective in application and that future rates may not be designed to recoup past losses in the absence of express legislative authority."[20] The Commission's decision to apply its asymmetrical pricing provisions on a going-forward basis only is not impermissible retroactive rate making.

This Court may not substitute its judgment for that of the Commission.[21] There is substantial evidence in the record to support the Commission's decision that Delaware ratepayers were not unduly prejudiced. The Commission's decision was neither arbitrary nor capricious. The Commission did not change previous rates. Thus, it did not engage in impermissible retroactive rate making. Furthermore, the Commission's decision to apply the rates prospectively is supported by substantial evidence on the record pursuant to 29 *Del. C.* § 10142(d).

Conclusion

For the foregoing reasons, the Court finds that there is substantial evidence to support the findings below, and that there was no error of law. The Commission exercised jurisdiction over Chesapeake for the limited purpose of regulating the rates charged by Chesapeake and PESCO to its direct sales customers and thus did not run

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[19] 468 A.2d 1285, 1299 (Del. 1983).

[20] *Id.*

[21] *Kreshtool v. Delmarva Power & Light Company*, 310 A.2d 649, 655 (Del. Super. 1973).

afoul to the FERC's jurisdiction. Substantial evidence exists to support the Commission's decision that Delaware ratepayers were not unfairly prejudiced by the Commission's prospective application of Order 7778. Accordingly, the decision of the Delaware Public Service Commission is **AFFIRMED**.

SO ORDERED this 13th day of June, 2011.

/s/ Robert B. Young
J.

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