

CHESAPEAKE UTILITIES CORP

Form 10-K

March 08, 2011

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

**FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the Fiscal Year Ended: December 31, 2010
Commission File Number: 001-11590**

**Chesapeake Utilities Corporation
(Exact name of registrant as specified in its charter)**

**State of Delaware
(State or other jurisdiction of
incorporation or organization)** **51-0064146
(I.R.S. Employer
Identification No.)**

**909 Silver Lake Boulevard, Dover, Delaware 19904
(Address of principal executive offices, including zip code)
302-734-6799**

**(Registrant's telephone number, including area code)
Securities registered pursuant to Section 12(b) of the Act:**

Title of each class	Name of each exchange on which registered
Common Stock par value per share \$0.4867	New York Stock Exchange, Inc.

**Securities registered pursuant to Section 12(g) of the Act:
8.25% Convertible Debentures Due 2014
(Title of class)**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendments to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of accelerated filer, large accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller Reporting Company
Indicate by a check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No .
The aggregate market value of the common shares held by non-affiliates of Chesapeake Utilities Corporation as of June 30, 2010, the last business day of its most recently completed second fiscal quarter, based on the last trade price on that date, as reported by the New York Stock Exchange, was approximately \$297.6 million.
As of February 28, 2011, 9,529,333 shares of common stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2011 Annual Meeting of Stockholders are incorporated by reference in Part II and Part III.

Chesapeake Utilities Corporation
Form 10-K
YEAR ENDED DECEMBER 31, 2010
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GLOSSARY OF KEY TERMS

Frequently used abbreviations, acronyms, or terms used in this report:

Subsidiaries of Chesapeake Utilities Corporation

BravePoint	BravePoint®, Inc., a wholly-owned subsidiary of Chesapeake Services Company, which is a wholly-owned subsidiary of Chesapeake
Chesapeake Company	The Registrant, the Registrant and its subsidiaries, or the Registrant's subsidiaries, as appropriate in the context of the disclosure
ESNG	Eastern Shore Natural Gas Company, a wholly-owned subsidiary of Chesapeake
FPU	Florida Public Utilities Company, a wholly-owned subsidiary of Chesapeake, effective October 28, 2009
PESCO	Peninsula Energy Services Company, Inc., a wholly-owned subsidiary of Chesapeake
PIPECO	Peninsula Pipeline Company, Inc., a wholly-owned subsidiary of Chesapeake
Sharp	Sharp Energy, Inc., a wholly-owned subsidiary of Chesapeake's and Sharp's subsidiary, Sharpgas, Inc.
Xeron	Xeron, Inc., a wholly-owned subsidiary of Chesapeake

Regulatory Agencies

Delaware PSC	Delaware Public Service Commission
DOT	United States Department of Transportation
EPA	United States Environmental Protection Agency
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
FDEP	Florida Department of Environmental Protection
Florida PSC	Florida Public Service Commission
IASB	International Accounting Standards Board
IRS	Internal Revenue Service
Maryland PSC	Maryland Public Service Commission
MDE	Maryland Department of the Environment
PSC	Public Service Commission
SEC	Securities and Exchange Commission

Accounting Standards Related

ASC	FASB Accounting Standards Codification™
ASU	FASB Accounting Standards Update
GAAP	Generally Accepted Accounting Principles
IFRS	International Financial Reporting Standards
FASB	Financial Accounting Standards Board

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Other

AS/SVE	Air Sparging and Soil/Vapor Extraction
BS/SVE	Bio-Sparging and Soil/Vapor Extraction
CDD	Cooling Degree-Days
Columbia	Columbia Gas Transmission, LLC
DSCP	Directors Stock Compensation Plan
Dts	Dekatherms
Dts/d	Dekatherms per Day
FCG	Florida City Gas
FGT	Florida Gas Transmission Company
FRP	Fuel Retention Percentage
GSR	Gas Sales Service Rates
Gulf	Columbia Gulf Transmission Company
Gulf Power	Gulf Power Company
Gulfstream	Gulfstream Natural Gas System, LLC
HDD	Heating Degree-Days
IGC	Indiantown Gas Company
Mcf	Thousand Cubic Feet
MGP	Manufactured Gas Plant
MWH	Megawatt Hour
NYSE	New York Stock Exchange
PIP	Performance Incentive Plan
RAP	Remedial Action Plan
S&P 500 Index	Standard & Poor's 500 Index
Sanford Group	FPU and Other Responsible Parties involved with the Sanford Environmental Site
TETLP	Texas Eastern Transmission, LP
Transco	Transcontinental Gas Pipe Line Company, LLC

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Part I

References in this document to Chesapeake, the Company, we, us and our mean Chesapeake Utilities Corporation and/or its wholly-owned subsidiaries, as appropriate in the context of the disclosure.

Safe Harbor for Forward-Looking Statements

We make statements in this Form 10-K that do not directly or exclusively relate to historical facts. Such statements are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. You can typically identify forward-looking statements by the use of forward-looking words, such as project, believe, expect, anticipate, intend, plan, estimate, continue, potential, forecast or other similar words, or future or conditional words such as may, will, should, would or could. These statements represent our intentions, plans, expectations, assumptions and beliefs about future financial performance, business strategy, projected plans and objectives of the Company.

These statements are subject to many risks and uncertainties. In addition to the risk factors described under Item 1A Risk Factors, the following important factors, among others, could cause actual future results to differ materially from those expressed in the forward-looking statements:

- state and federal legislative and regulatory initiatives that affect cost and investment recovery, have an impact on rate structures, and affect the speed at and degree to which competition enters the electric and natural gas industries (including deregulation);
- the outcomes of regulatory, tax, environmental and legal matters, including whether pending matters are resolved within current estimates;
- industrial, commercial and residential growth or contraction in our service territories;
- the weather and other natural phenomena, including the economic, operational and other effects of hurricanes and ice storms;
- the timing and extent of changes in commodity prices and interest rates;
- general economic conditions, including any potential effects arising from terrorist attacks and any consequential hostilities, other hostilities or other external factors over which we have no control;
- changes in environmental and other laws and regulations to which we are subject;
- the results of financing efforts, including our ability to obtain financing on favorable terms, which can be affected by various factors, including credit ratings and general economic conditions;
- declines in the market prices of equity securities and resultant cash funding requirements for our defined benefit pension plans;
- the creditworthiness of counterparties with which we are engaged in transactions;
- growth in opportunities for our business units;
- the extent of success in connecting natural gas and electric supplies to transmission systems and in expanding natural gas and electric markets;
- the effect of accounting pronouncements issued periodically by accounting standard-setting bodies;
- conditions of the capital markets and equity markets during the periods covered by the forward-looking statements;
- the ability to successfully execute, manage and integrate merger, acquisition or divestiture plans, regulatory or other limitations imposed as a result of a merger, acquisition or divestiture, and the success of the business following a merger, acquisition or divestiture;
- the ability to manage and maintain key customer relationships;
- the ability to maintain key supply sources;

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the effect of spot, forward and future market prices on our distribution, wholesale marketing and energy trading businesses;
the effect of competition on our businesses;
the ability to construct facilities at or below estimated costs;
changes in technology affecting our advanced information services business; and
operational and litigation risks that may not be covered by insurance.

Item 1. Business.**(a) Overview**

We are a diversified utility company engaged in various energy and other businesses. Chesapeake is a Delaware corporation that was formed in 1947. On October 28, 2009, we completed a merger with Florida Public Utilities Company (FPU), pursuant to which FPU became a wholly-owned subsidiary of Chesapeake. We operate regulated energy businesses through our natural gas distribution divisions in Delaware, Maryland and Florida, natural gas and electric distribution operations in Florida through FPU, and natural gas transmission operations on the Delmarva Peninsula and Florida through our subsidiaries, Eastern Shore Natural Gas Company (ESNG) and Peninsula Pipeline Company, Inc. (PIPECO), respectively. Our unregulated businesses include our natural gas marketing operation through Peninsula Energy Services Company, Inc. (PESCO); propane distribution operations through Sharp Energy, Inc. and its subsidiary Sharpgas, Inc. (collectively Sharp) and FPU's propane distribution subsidiary, Flo-Gas Corporation; and our propane wholesale marketing operation through Xeron, Inc. (Xeron). We also have an advanced information services subsidiary, BravePoint, Inc. (BravePoint).

(b) Operating Segments

We are composed of three operating segments:

Regulated Energy. The regulated energy segment includes natural gas distribution, electric distribution and natural gas transmission operations. All operations in this segment are regulated, as to their rates and services, by the Public Service Commission (PSC) having jurisdiction in each operating territory or by the Federal Energy Regulatory Commission (FERC) in the case of ESNG.

Unregulated Energy. The unregulated energy segment includes natural gas marketing, propane distribution and propane wholesale marketing operations, which are unregulated as to their rates and services.

Other. The other segment consists primarily of the advanced information services operation, unregulated subsidiaries that own real estate leased to Chesapeake and certain corporate costs not allocated to other operations.

The following table shows the size of each of our operating segments based on operating income for 2010 and net property, plant and equipment as of December 31, 2010:

<i>(in thousands)</i>	Operating Income		Net Property, Plant & Equipment	
Regulated Energy	\$ 43,509	84%	\$ 414,622	90%
Unregulated Energy	7,908	15%	35,658	8%
Other	513	1%	12,477	2%
Total	\$ 51,930	100%	\$ 462,757	100%

Additional financial information by business segment is included in Item 8 under the heading Notes to the Consolidated Financial Statements Note C, Segment Information.

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Our regulated energy segment provides natural gas distribution services in Delaware, Maryland and Florida, electric distribution services in Florida and natural gas transmission services in Delaware, Maryland, Pennsylvania and Florida.

Natural Gas Distribution

Natural gas supplies nearly one-fourth of the energy used in the United States. Due to its efficiency, cleanliness and reliability, natural gas is growing increasingly popular. With 99 percent of the natural gas consumed in the United States coming from North America, supplies of natural gas are abundant. Natural gas is delivered to customers through a safe and efficient underground pipeline system. As the cleanest-burning fossil fuel, increased use of natural gas can help address various environmental concerns today.

Our Delaware and Maryland natural gas distribution divisions serve 52,686 residential and commercial customers and 177 industrial customers in central and southern Delaware and Maryland's Eastern Shore. For the year ended December 31, 2010, operating revenues and deliveries by customer class for our Delaware and Maryland distribution divisions were as follows:

	Operating Revenues		Deliveries	
	<i>(in thousands)</i>		<i>(Mcf s)</i>	
Residential	\$ 46,041	57%	2,881,073	35%
Commercial	27,896	34%	2,145,143	26%
Industrial	3,766	5%	3,020,907	36%
Subtotal	77,703	96%	8,047,123	97%
Interruptible	655	1%	232,653	3%
Other ⁽¹⁾	2,507	3%		
Total	\$ 80,865	100%	8,279,776	100%

⁽¹⁾ Operating revenues from other include unbilled revenue, rental of gas properties, and other miscellaneous charges.

Our Florida natural gas distribution operations consist of Chesapeake's Florida division and FPU's natural gas operation, which was acquired in the merger with FPU in October 2009. In August 2010, FPU added a new division through the purchase of the natural gas operating assets of Indiantown Gas Company (IGC). On a combined basis, our Florida natural gas distribution operations serve 61,053 residential customers and 6,314 commercial and industrial customers in 20 counties in Florida. For the year ended December 31, 2010, operating revenues and deliveries by customer class for our Florida natural gas distribution operations were as follows:

	Operating Revenues		Deliveries	
	<i>(in thousands)</i>		<i>(Mcf s)</i>	
Residential	\$ 27,742	35%	1,716,934	8%
Commercial	39,006	48%	4,451,414	20%
Industrial	13,043	16%	15,582,234	72%
Other ⁽¹⁾	607	1%	12,723	
Total	\$ 80,398	100%	21,763,305	100%

- (1) Operating revenues from other include unbilled revenue, conservation revenue, fees for billing services provided to third parties and other miscellaneous charges.

Table of Contents**Electric Distribution**

Our Florida electric distribution operation, which was acquired in the FPU merger, distributes electricity to 30,966 customers in four counties in northeast and northwest Florida. For the year ended December 31, 2010, operating revenues and deliveries by customer class for the FPU electric distribution operation were as follows:

	Operating Revenues <i>(in thousands)</i>		Deliveries <i>(MWHs)</i>	
Residential	\$ 51,498	55%	347,040	47%
Commercial	45,332	48%	332,322	45%
Industrial	7,705	8%	66,580	9%
Subtotal	104,535	111%	745,942	101%
Other ⁽¹⁾	(10,452)	(11%)	(6,286)	(1%)
Total	\$ 94,083	100%	739,656	100%

⁽¹⁾ Operating revenues from other include unbilled revenue, under (over) recoveries of fuel cost, conservation revenue, other miscellaneous charges and adjustments for pass-through taxes.

Natural Gas Transmission

ESNG operates a 396-mile interstate pipeline system that transports natural gas from various points in Pennsylvania to Chesapeake's Delaware and Maryland natural gas distribution divisions, as well as to other utilities and industrial customers in southern Pennsylvania, Delaware and on the Eastern Shore of Maryland. ESNG also provides swing transportation service and contract storage services. For the year ended December 31, 2010, operating revenues and deliveries by customer class for ESNG were as follows:

	Operating Revenues <i>(in thousands)</i>		Deliveries <i>(Mcf)</i>	
Local distribution companies	\$ 20,441	76%	10,848,108	62%
Industrial	4,864	18%	4,794,442	27%
Commercial	1,571	6%	1,962,890	11%
Other ⁽¹⁾	41	0%		
Subtotal	26,917	100%	17,605,440	100%
Less: affiliated local distribution companies	(12,903)	(48%)	(5,853,083)	(33%)
Total non-affiliated	\$ 14,014	52%	11,752,357	67%

⁽¹⁾ Operating revenues from other sources are from rental of gas properties.

PIPECO currently provides natural gas transportation services to a customer for a period of 20 years beginning in January 2009 at a fixed monthly charge, through an eight-mile pipeline located in Suwanee County, Florida, which PIPECO owns. For the year ended December 31, 2010, PIPECO had \$264,000 in operating revenues under the contract.

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Supplies, Transmission and Storage

We believe that the availability of supply and transmission of natural gas and electricity is adequate under existing arrangements to meet the anticipated needs of customers.

Natural Gas Distribution- Delaware and Maryland

Our Delaware and Maryland natural gas distribution divisions have both firm and interruptible transportation service contracts with five interstate open access pipeline companies, including the ESNG pipeline. These divisions are directly interconnected with the ESNG pipeline, and have contracts with interstate pipelines upstream of ESNG, including Transcontinental Gas Pipe Line Company LLC (Transco), Columbia Gas Transmission LLC (Columbia), Columbia Gulf Transmission Company (Gulf) and Texas Eastern Transmission, LP (TETLP). The Transco, Columbia and TETLP pipelines are directly interconnected with the ESNG pipeline. The Gulf pipeline is directly interconnected with the Columbia pipeline and indirectly interconnected with the ESNG pipeline. None of the upstream pipelines is owned or operated by an affiliate of the Company.

On April 8, 2010, our Delaware and Maryland divisions entered into a Precedent Agreement with TETLP in conjunction with TETLP's new expansion project. Upon satisfaction of certain conditions provided in the Precedent Agreement, the Delaware and Maryland divisions will execute two firm transportation service contracts, one for our Delaware division for 28,986 Mcfs per day and one for our Maryland division for 9,662 Mcfs per day, to be effective on the service commencement date of the project, which is currently projected to occur in November 2012. The new firm transportation service contracts between our Delaware and Maryland divisions and TETLP will provide us with an additional direct interconnection with ESNG's transmission system and access to new sources of natural gas supplies from other natural gas production regions, including the Appalachian production region, thereby providing increased reliability and diversity of supply. They will also provide our Delaware and Maryland divisions with additional upstream transportation capacity to meet current customer demands and to plan for sustainable growth. In December 2010, ESNG completed its mainline extension to interconnect with the TETLP pipeline. Until TETLP's expansion project is completed, our Delaware and Maryland divisions expect to utilize currently available capacity on a portion of TETLP's existing pipeline. For the 2010 and 2011 winter season, our Delaware and Maryland divisions have contracted for 14,493 Mcfs per day and 4,831 Mcfs per day, respectively, from TETLP.

The Delaware and Maryland divisions use their firm transportation supply resources to meet a significant percentage of their projected demand requirements and they purchase natural gas supplies on the spot market from various suppliers as needed to match firm supply and demand. This gas is transported by the upstream pipelines and delivered to their interconnections with ESNG. These divisions also have the capability to use propane-air peak-shaving to supplement or displace spot market purchases.

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The following table shows the firm transportation and storage capacity that the Delaware and Maryland divisions currently have under contract with ESNG and pipelines upstream of the ESNG pipeline, including the respective contract expiration dates.

Delaware

Pipeline	Firm transportation capacity maximum peak-day daily deliverability (Mcfs)	Firm storage capacity maximum peak-day daily withdrawal (Mcfs)	Expiration
Transco	20,699	6,190	Various dates between 2012 and 2028
Columbia	17,836	7,946	Various dates between 2011 and 2020
Gulf	850		Expires in 2014
TETLP	14,493		Expires in 2012
ESNG	64,602	4,006	Various dates between 2011 and 2027

Maryland

Pipeline	Firm transportation capacity maximum peak-day daily deliverability (Mcfs)	Firm storage capacity maximum peak-day daily withdrawal (Mcfs)	Expiration
Transco	5,921	2,909	Various dates between 2012 and 2013
Columbia	6,473	3,539	Various dates between 2011 and 2018
Gulf	570		Expires in 2014
TETLP	4,831		Expires in 2012
ESNG	21,380	2,228	Various dates between 2011 and 2027

The Delaware and Maryland divisions currently have contracts with several suppliers for the purchase of firm natural gas supply in the amount of their capacities on the Transco and Columbia pipelines.

Natural Gas Distribution- Florida

Chesapeake's Florida natural gas distribution division has firm transportation service contracts with Florida Gas Transmission Company (FGT) and Gulfstream Natural Gas System, LLC (Gulfstream). Pursuant to a program approved by the Florida Public Service Commission (Florida PSC), all of the capacity under these agreements has been released to various third-parties, including PESCO. Under the terms of these capacity release agreements, Chesapeake is contingently liable to FGT and Gulfstream, should any party that acquired the capacity through release fail to pay for the service.

Contracts by Chesapeake's Florida natural gas distribution division with FGT include: (a) a contract, which expires on July 31, 2012, for daily firm transportation capacity of 17,175 Mcfs for the months of November through April, capacity of 14,695 Mcfs for the months of May through September, and 16,143 Mcfs for October; and (b) a contract

for daily firm transportation capacity of 974 Mcfs daily, which expires in 2015. Chesapeake's contract with Gulfstream is for daily firm transportation capacity of 9,737 Mcfs and expires in 2022.

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FPU has the following firm transportation contracts with FGT:

(a) two contracts expiring in July 2020 for daily firm transportation capacity of:

	Daily Firm Transportation Capacity (in Mcfs)
January March	28,647
April	24,156
May September	9,681
October	10,210
November December	28,647

(b) one contract expiring in February 2015 for daily firm transportation capacity of:

	Daily Firm Transportation Capacity (in Mcfs)
January April	10,286
May October	4,360
November December	10,286

(c) one contract for daily firm transportation capacity of 1,774 Mcfs with various partial expiration dates between 2016 and 2023.

FPU also has a firm transportation contract with Florida City Gas (FCG), expiring in 2013, which provides daily firm transportation capacity of 292 Mcfs on its Pioneer Pipeline, and a firm transportation contract with IGC, expiring in 2016, which provides daily firm transportation capacity of 487 Mcfs on its distribution system.

FPU uses gas marketers and producers to procure all of its gas supplies for its natural gas distribution operations. FPU also uses TECO Peoples Gas to provide wholesale gas sales service in areas distant from its interconnections with FGT.

Natural Gas Transmission

ESNG has three contracts with Transco for a total of 7,045 Mcfs of firm peak day storage entitlements and total storage capacity of 278,264 Mcfs, each of which expires in 2013. ESNG has retained these firm storage services in order to provide swing transportation service and firm storage service to those customers that have requested such services.

Electric Distribution

Our electric distribution operation through FPU purchases all of its wholesale electricity from two suppliers: Gulf Power Company (Gulf Power) and JEA (formerly known as Jacksonville Electric Authority). Both of these contracts are all requirement contracts and they expire in December 2019 and December 2017, respectively. The JEA contract provides generation, transmission and distribution service to northeast Florida. The Gulf Power contract provides generation, transmission and distribution service to northwest Florida.

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See discussion of competition in Item 7 under the heading Management's Discussion and Analysis of Financial Condition and Results of Operations - Competition.

Rates and Regulation

Our natural gas and electric distribution operations are subject to regulation by the Delaware, Maryland and Florida PSCs with respect to various aspects of their business, including rates for sales and transportation to all customers in each respective jurisdiction. All of our firm distribution sales rates are subject to fuel cost recovery mechanisms, which match revenues with natural gas and electric supply and transportation costs and normally allow full recovery of such costs. Adjustments under these mechanisms, which are limited to such costs, require periodic filings and hearings with the state regulatory authority having jurisdiction.

ESNG is subject to regulation as an interstate pipeline by the FERC, which regulates the terms and conditions of service and the rates ESNG can charge for its transportation and storage services. PIPECO is subject to regulation by the Florida PSC.

The following table shows the regulatory jurisdictions under which our regulated energy businesses currently operate, including the effective dates of the most recent full rate proceedings and the rates of return that were authorized therein:

Regulated Business	Regulatory Jurisdiction	Effective Date of the Current Rates	Allowed Return
Chesapeake - Delaware Division	Delaware PSC	9/3/2008	10.25% (1)
Chesapeake - Maryland Division	Maryland PSC	12/1/2007	10.75% (1)
Chesapeake - Florida Division	Florida PSC	1/14/2010	10.80% (1)
FPU - Natural Gas	Florida PSC	1/14/2010 ⁽³⁾	10.85% (1)
FPU - Electric	Flori		