CHESAPEAKE UTILITIES CORP
Form 10-Q
August 07, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: June 30, 2014

OR

.. TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number: 001-11590

CHESAPEAKE UTILITIES CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	51-0064146
(State or other jurisdiction of incorporation or organization)	(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)

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 x 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 x No ¨

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 definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

Common Stock, par value $0.4867 — 9,714,994 shares outstanding as of July 31, 2014.

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GLOSSARY OF DEFINITIONS

ASC: Accounting Standards Codification
ASU: Accounting Standards Update
Austin Cox: Austin Cox Home Services, Inc.
BravePoint: BravePoint®, Inc., our advanced information services subsidiary, headquartered in Norcross, Georgia
CDD: Cooling degree-days, which is the measure of the variation in weather based on the extent to which the daily average temperature (from 10:00 am to 10:00 am) is above 65 degrees Fahrenheit
Chesapeake: Chesapeake Utilities Corporation, its divisions and its subsidiaries, as appropriate in the context of the disclosure
Chesapeake Pension Plan: A defined benefit pension plan sponsored by Chesapeake
Chesapeake Postretirement Plan: An unfunded postretirement health care and life insurance plan sponsored by Chesapeake
Chesapeake SERP: An unfunded supplemental executive retirement pension plan sponsored by Chesapeake
Company: Chesapeake Utilities Corporation, its divisions and its subsidiaries, as appropriate in the context of the disclosure
CP: Certificate of Public Convenience and Necessity
Deferred Compensation Plan: A non-qualified, deferred compensation arrangement under which certain of our executives and members of the Board of Directors are able to defer payment of all or a part of certain specified types of compensation, including executive cash bonuses, executive performance shares, and directors' retainers and fees
Delmarva Peninsula: A peninsula on the east coast of the United States of America occupied by Delaware and portions of Maryland and Virginia
DNREC: Delaware Department of Natural Resources and Environmental Control
DSCP: Directors Stock Compensation Plan
Dts/d: Dekatherms per day
Eastern Shore: Eastern Shore Natural Gas Company, a wholly-owned natural gas transmission subsidiary of Chesapeake
EGWIC: Eastern Gas & Water Investment Company, LLC, an affiliate of Eastern Shore Gas Company
EPA: United States Environmental Protection Agency
ESG: Eastern Shore Gas Company and its affiliates
FASB: Financial Accounting Standards Board
FERC: Federal Energy Regulatory Commission, an independent agency of the Federal government that regulates the interstate transmission of electricity, natural gas, and oil
FDEP: Florida Department of Environmental Protection
FDOT: Florida Department of Transportation
FGT: Florida Gas Transmission Company
FPU: Florida Public Utilities Company, a wholly-owned subsidiary of Chesapeake
FPU Medical Plan: A separate unfunded postretirement medical plan for FPU sponsored by Chesapeake
FPU Pension Plan: A separate defined benefit pension plan for FPU sponsored by Chesapeake
FRP: Fuel Retention Percentage

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GAAP: Accounting principles generally accepted in the United States of America
Glades: Glades Gas Co., Inc.
GRIP: Gas Reliability Infrastructure Program, which is a surcharge to natural gas customers designed to recover capital and other program-related costs, inclusive of an appropriate return on investment, associated with accelerating the replacement of qualifying distribution mains and services in Florida
Gulf Power: Gulf Power Company
Gulfstream: Gulfstream Natural Gas System, LLC
HDD: Heating degree-days, which is a measure of the variation in weather based on the extent to which the daily average temperature (from 10:00 am to 10:00 am) is below 65 degrees Fahrenheit
MDE: Maryland Department of Environment
MGP: Manufactured gas plant, which is a site where coal was previously used to manufacture gaseous fuel for industrial, commercial and residential use
NAM: Natural Attenuation Monitoring
Note Agreement: Note Purchase Agreement entered into by Chesapeake with Note Holders on September 5, 2013
Note Holders: PAR U Hartford Life & Annuity Comfort Trust, The Prudential Insurance Company of America, The Gibraltar Life Insurance Co., Ltd., The Penn Mutual Life Insurance Company, Thrivent Financial for Lutherans, United of Omaha Life Insurance Company, and Companion Life Insurance Company, which are collectively the lenders that entered into the Note Agreement with Chesapeake on September 5, 2013
Notes: Series A and B unsecured Senior Notes that have been or will be entered into with the Note Holders
OTC: Over-the-counter
Peninsula Pipeline: Peninsula Pipeline Company, Inc., our wholly-owned Florida intrastate pipeline subsidiary
PESCO: Peninsula Energy Services Company, Inc., our wholly-owned natural gas marketing subsidiary
PIP: Performance Incentive Plan
PSC: Public Service Commission, which is the state agency that regulates the rates and services provided by Chesapeake's natural gas and electric distribution operations in Delaware, Maryland and Florida and Peninsula Pipeline in Florida
Sandpiper: Sandpiper Energy, Inc.
Sanford Group: FPU and other responsible parties involved with the Sanford environmental site
SEC: Securities and Exchange Commission
Series A Notes: Series A of the unsecured Senior Notes issued on December 16, 2013 pursuant to the Note Agreement
Series B Notes: Series B of the unsecured Senior Notes issued on May 15, 2014 pursuant to the Note Agreement
Sharp: Sharp Energy, Inc., our wholly-owned propane distribution subsidiary
SICP: 2013 Stock and Incentive Compensation Plan, which replaced DSCP and PIP effective May 2, 2013
TETLP: Texas Eastern Transmission, LP
Xeron: Xeron, Inc., our propane wholesale marketing subsidiary, based in Houston, Texas

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PART I—FINANCIAL INFORMATION
Item 1. Financial Statements
Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Statements of Income (Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
(in thousands, except shares and per share data)				
Operating Revenues				
Regulated energy	$61,646	$55,216	$163,812	$136,783
Unregulated energy	34,321	36,025	114,294	91,016
Other	4,530	2,905	8,728	7,075
Total Operating Revenues	100,497	94,146	286,834	234,874
Operating Expenses				
Regulated energy cost of sales	24,672	22,115	78,979	63,730
Unregulated energy and other cost of sales	28,442	28,773	89,766	68,861
Operations	24,615	22,822	51,242	44,577
Maintenance	2,457	1,820	4,606	3,542
Depreciation and amortization	6,736	5,977	13,371	11,797
Other taxes	3,118	3,487	6,791	6,665
Total Operating Expenses	90,040	84,994	244,755	199,172
Operating Income	10,457	9,152	42,079	35,702
Other income, net of other expenses	405	24	413	312
Interest charges	2,303	2,016	4,459	4,088
Income Before Income Taxes	8,559	7,160	38,033	31,926
Income taxes	3,425	2,804	15,218	12,701
Net Income	$5,134	$4,356	$22,815	$19,225
Weighted Average Common Shares Outstanding:				
Basic	9,704,161	9,621,580	9,681,422	9,611,610
Diluted	9,737,852	9,695,470	9,715,762	9,687,253
Earnings Per Share of Common Stock:				
Basic	$0.53	$0.45	$2.36	$2.00
Diluted	$0.53	$0.45	$2.35	$1.99
Cash Dividends Declared Per Share of Common Stock	$0.405	$0.385	$0.790	$0.750

The accompanying notes are an integral part of these financial statements.

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Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Statements of Comprehensive Income (Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
(in thousands)				
Net Income	$5,134	$4,356	$22,815	$19,225
Other Comprehensive Income, net of tax:				
Employee Benefits, net of tax:				
Amortization of prior service cost, net of tax of ($6), ($6), ($12), and ($12) respectively	(9)	(9)	(18)	(18)
Net gain, net of tax of $27, $43, $53 and $81, respectively	40	64	79	122
Cash Flow Hedges, net of tax:				
Unrealized loss on commodity contract cash flow hedges, net of tax of ($1), $0, ($1) and $0, respectively.	(1)	—	(1)	—
Total other comprehensive income	30	55	60	104
Comprehensive Income	$5,164	$4,411	$22,875	$19,329

The accompanying notes are an integral part of these financial statements.

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Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Balance Sheets (Unaudited)

Assets	June 30, 2014	December 31, 2013
(in thousands, except shares)		
Property, Plant and Equipment		
Regulated energy	$710,444	$691,522
Unregulated energy	78,616	76,267
Other	21,677	21,002
Total property, plant and equipment	810,737	788,791
Less: Accumulated depreciation and amortization	(186,663)	(174,148)
Plus: Construction work in progress	36,615	16,603
Net property, plant and equipment	660,689	631,246
Current Assets		
Cash and cash equivalents	2,529	3,356
Accounts receivable (less allowance for uncollectible accounts of $1,819 and $1,635, respectively)	44,858	75,293
Accrued revenue	7,631	13,910
Propane inventory, at average cost	6,836	10,456
Other inventory, at average cost	3,382	4,880
Storage gas prepayments	3,131	4,318
Prepaid expenses	4,229	6,910
Income taxes receivable	—	2,609
Mark-to-market energy assets	136	385
Regulatory assets	5,822	2,436
Deferred income taxes	1,657	1,696
Other current assets	203	160
Total current assets	80,414	126,409
Deferred Charges and Other Assets		
Investments, at fair value	3,542	3,098
Regulatory assets	66,300	66,584
Goodwill	4,625	4,354
Other intangible assets, net	2,775	2,975
Receivables and other deferred charges	2,740	2,856
Total deferred charges and other assets	79,982	79,867
Total Assets	$821,085	$837,522

The accompanying notes are an integral part of these financial statements.

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Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Balance Sheets (Unaudited)

Capitalization and Liabilities	June 30, 2014	December 31, 2013
(in thousands, except shares and per share data)		
Capitalization		
Stockholders' equity		
Common stock, par value $0.4867 per share (authorized 25,000,000 shares)	$4,727	$4,691
Additional paid-in capital	154,619	152,341
Retained earnings	139,350	124,274
Accumulated other comprehensive loss	(2,473)	(2,533)
Deferred compensation obligation	1,202	1,124
Treasury stock	(1,202)	(1,124)
Total stockholders' equity	296,223	278,773
Long-term debt, net of current maturities	165,370	117,592
Total capitalization	461,593	396,365
Current Liabilities		
Current portion of long-term debt	11,117	11,353
Short-term borrowing	47,870	105,666
Accounts payable	30,184	53,482
Accrued compensation	5,495	8,394
Accrued interest	1,352	1,235
Dividends payable	3,933	3,710
Income taxes payable	695	—
Mark-to-market energy liabilities	32	127
Regulatory liabilities	5,875	4,157
Customer deposits and refunds	23,482	26,140
Other accrued liabilities	9,978	7,678
Total current liabilities	140,013	221,942
Deferred Credits and Other Liabilities		
Deferred income taxes	142,766	142,597
Deferred investment tax credits	57	74
Regulatory liabilities	3,975	4,402
Accrued asset removal cost—Regulatory liability	39,991	39,510
Environmental liabilities	9,076	9,155
Other pension and benefit costs	20,123	21,000
Other liabilities	3,491	2,477
Total deferred credits and other liabilities	219,479	219,215
Other commitments and contingencies (Note 6)		
Total Capitalization and Liabilities	$821,085	$837,522

The accompanying notes are an integral part of these financial statements.

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Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)

	Six Months Ended June 30,	
	2014	2013
(in thousands)		
Operating Activities		
Net income	$22,815	$19,225
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13,371	11,797
Depreciation and accretion included in other costs	3,447	3,030
Deferred income taxes, net	166	5,796
Gain on sale of assets	(420)	(39)
Unrealized (gain) loss on commodity contracts	62	(153)
Unrealized gain on investments	(152)	(42)
Realized gain on sales of investments, net	—	(310)
Employee benefits	319	458
Share-based compensation	1,065	861
Other, net	(1)	(22)
Changes in assets and liabilities:		
Purchase of investments	(293)	(398)
Accounts receivable and accrued revenue	36,713	(6,268)
Propane inventory, storage gas and other inventory	6,074	2,180
Regulatory assets	(5,250)	1,721
Prepaid expenses and other current assets	3,183	2,312
Accounts payable and other accrued liabilities	(22,491)	8,074
Income taxes receivable and payable	3,305	6,599
Accrued interest	118	(316)
Customer deposits and refunds	(2,658)	(3,958)
Accrued compensation	(2,975)	(2,060)
Regulatory liabilities	1,761	5,588
Other assets and liabilities, net	63	(12)
Net cash provided by operating activities	58,222	54,063
Investing Activities		
Property, plant and equipment expenditures	(42,753)	(41,220)
Proceeds from sales of assets	459	45
Acquisitions	—	(19,541)
Environmental expenditures	(79)	(209)
Net cash used in investing activities	(42,373)	(60,925)
Financing Activities		
Common stock dividends	(6,754)	(6,356)
Purchase of stock for Dividend Reinvestment Plan	(392)	(655)
Change in cash overdrafts due to outstanding checks	(806)	(1,240)
Net borrowing (repayment) under line of credit agreements	(56,990)	15,532
Proceeds from issuance of long-term debt	50,000	7,000
Repayment of long-term debt and capital lease obligation	(1,734)	(8,570)
Net cash provided by (used in) financing activities	(16,676)	5,711
Net Decrease in Cash and Cash Equivalents	(827)	(1,151)
Cash and Cash Equivalents—Beginning of Period	3,356	3,361

Cash and Cash Equivalents—End of Period	$2,529	$2,210

The accompanying notes are an integral part of these financial statements.

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Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Statements of Stockholders' Equity (Unaudited)

(in thousands, except shares and per share data)	Common Stock Number of Shares[1]	Common Stock Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Deferred Compensation	Treasury Stock	Total
Balance at December 31, 2012	9,597,499	$4,671	$150,750	$106,239	$ (5,062)	$ 982	$(982)	$256,598
Net Income	—	—	—	32,787	—	—	—	32,787
Other comprehensive income	—	—	—	—	2,529	—	—	2,529
Dividend declared ($1.520 per share)	—	—	(6)	(14,752)	—	—	—	(14,758)
Conversion of debentures	17,383	8	287	—	—	—	—	295
Share-based compensation and tax benefit [2] [3]	23,348	12	1,310	—	—	—	—	1,322
Treasury stock activities	—	—	—	—	—	142	(142)	—
Balance at December 31, 2013	9,638,230	4,691	152,341	124,274	(2,533)	1,124	(1,124)	278,773
Net Income	—	—	—	22,815	—	—	—	22,815
Other comprehensive income	—	—	—	—	60	—	—	60
Dividend declared ($0.790 per share)	5,193	3	318	(7,739)	—	—	—	(7,418)
Retirement Savings Plan	9,834	5	597	—	—	—	—	602
Conversion of debentures	31,542	15	520	—	—	—	—	535
Share-based compensation and tax benefit [2] [3]	26,772	13	843	—	—	—	—	856
Treasury stock activities	—	—	—	—	—	78	(78)	—
Balance at June 30, 2014	9,711,571	$4,727	$154,619	$139,350	$ (2,473)	$ 1,202	$(1,202)	$296,223

(1) Includes 34,960 and 34,495 shares at June 30, 2014 and December 31, 2013, respectively, held in a Rabbi Trust related to our Non-Qualified Deferred Compensation Plan.
(2) Includes amounts for shares issued for Directors' compensation.
(3) The shares issued under the SICP are net of shares withheld for employee taxes. For the quarter ended June 30, 2014 and for the year ended December 31, 2013, we withheld 8,458 and 10,411 shares, respectively, for taxes.

The accompanying notes are an integral part of these financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Summary of Accounting Policies

Basis of Presentation

References in this document to the "Company," "Chesapeake," "we," "us" and "our" are intended to mean Chesapeake Utilitie Corporation, its divisions and/or its subsidiaries, as appropriate in the context of the disclosure.

The accompanying unaudited condensed consolidated financial statements have been prepared in compliance with the rules and regulations of the SEC and GAAP. In accordance with these rules and regulations, certain information and disclosures normally required for audited financial statements have been condensed or omitted. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto, included in our latest Annual Report on Form 10-K for the year ended December 31, 2013. In the opinion of management, these financial statements reflect normal recurring adjustments that are necessary for a fair presentation of our results of operations, financial position and cash flows for the interim periods presented.

Due to the seasonality of our business, results for interim periods are not necessarily indicative of results for the entire fiscal year. Revenue and earnings are typically greater during the first and fourth quarters, when consumption of energy is highest due to colder temperatures.

Stock Dividend

On July 2, 2014, our Board of Directors approved a three-for-two stock split of our outstanding common stock to be effected in the form of a stock dividend. Each stockholder as of the close of business on the record date of August 13, 2014 will receive one additional share of common stock for every two shares of common stock owned. The stock dividend will be issued on September 8, 2014.

FASB Statements and Other Authoritative Pronouncements

Recent Accounting Standards Yet to be Adopted

Revenue from Contracts with Customers (ASC 606) - In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This standard provides a single comprehensive revenue recognition model for all contracts with customers to improve comparability within industries, as well as across industries and capital markets. The standard contains principles that entities will apply to determine the measurement of revenue and when it is recognized. ASU 2014-09 is effective for reporting periods (interim and annual) beginning after December 15, 2016. We are currently assessing the impact this standard will have on our financial position and results of operations.

Recently Adopted Accounting Standards

Income Taxes (ASC 740) - In July 2013, the FASB issued ASU 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists, which requires the netting of certain unrecognized tax benefits against a deferred tax asset for a loss or other similar tax carryforward that would apply upon settlement of an uncertain tax position. ASU 2013-11 became effective for us on January 1, 2014. The adoption of ASU 2013-11 had no material impact on our financial position and results of operations.

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2. Calculation of Earnings Per Share

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
(in thousands, except shares and per share data)				
Calculation of Basic Earnings Per Share:				
Net Income	$5,134	$4,356	$22,815	$19,225
Weighted average shares outstanding	9,704,161	9,621,580	9,681,422	9,611,610
Basic Earnings Per Share	$0.53	$0.45	$2.36	$2.00
Calculation of Diluted Earnings Per Share:				
Reconciliation of Numerator:				
Net Income	$5,134	$4,356	$22,815	$19,225
Effect of 8.25% Convertible debentures (1)	—	11	—	22
Adjusted numerator—Diluted	$5,134	$4,367	$22,815	$19,247
Reconciliation of Denominator:				
Weighted shares outstanding—Basic	9,704,161	9,621,580	9,681,422	9,611,610
Effect of dilutive securities:				
Share-based Compensation	33,691	22,454	34,340	22,789
8.25% Convertible debentures (1)	—	51,436	—	52,854
Adjusted denominator—Diluted	9,737,852	9,695,470	9,715,762	9,687,253
Diluted Earnings Per Share	$0.53	$0.45	$2.35	$1.99

(1) As of March 1, 2014, we no longer have any outstanding convertible debentures. See Note 14, Long-term debt for additional information.

3. Acquisitions

Eastern Shore Gas Company

On May 31, 2013, the Maryland PSC approved the acquisition of ESG. Upon receiving this approval, we completed the purchase of certain operating assets of ESG, which was not related to, or affiliated with, our interstate natural gas transmission subsidiary, Eastern Shore. We paid approximately $16.5 million at the closing of the transaction, which was subject to certain adjustments specified in the asset purchase agreement. During the third quarter of 2013, the purchase price was reduced by $543,000 due to adjustments to property, plant and equipment, propane inventory, accounts receivable and other accrued liabilities. The purchase price included approximately $726,000 of sales tax related to the transaction. We financed the acquisition using unsecured short-term debt.

Approximately 11,000 residential and commercial underground propane distribution system customers and 500 bulk propane delivery customers acquired in the transaction are being served by our new subsidiary, Sandpiper, and our propane distribution subsidiary, Sharp, respectively. Sandpiper's operations, which cover all of Worcester County, Maryland, are now subject to rate and service regulation by the Maryland PSC. We are evaluating the potential conversion of some of the underground propane distribution systems to natural gas distribution and have begun to convert some of the acquired customers. Although most of these customers are currently being served with propane, we classify Sandpiper's operations as natural gas distribution in the Regulated Energy segment.

In connection with this acquisition, we recorded $12.6 million in property, plant and equipment, $384,000 in propane inventory, $2.5 million in accounts receivable and accrued revenue and $227,000 in other current liabilities, which included the effect of purchase price adjustments in the third quarter of 2013 and the second quarter of 2014. All but insignificant amounts of assets and liabilities are recorded in the Regulated Energy segment. No goodwill or intangible asset was recorded from this acquisition. The allocation of the purchase price and valuation of assets are final, as the final purchase price allocation was completed.

The revenue from this acquisition for the three and six months ended June 30, 2014, included in our condensed consolidated statement of income, were $4.2 million and $14.4 million, respectively. The net income from this acquisition for the three and six months ended June 30, 2014, included in our condensed consolidated statement of income, were $123,000 and $1.8 million, respectively.

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Other Acquisitions

On December 2, 2013, we acquired certain operating assets of the City of Fort Meade, Florida, for approximately $792,000. The purchased assets are used to provide natural gas distribution service in the City of Fort Meade, Florida. In connection with this acquisition, we recorded $670,000 in property, plant and equipment, $14,000 in inventory, $150,000 in goodwill and $42,000 in other current liabilities. Valuation of certain property, plant and equipment is preliminary and may be adjusted in the future based upon the final valuation, but no later than one year from the date of acquisition. All of the goodwill is expected to be deductible for income tax purposes. The revenue and net income from this acquisition that were included in our condensed consolidated statement of income for the three and six months ended June 30, 2014 were not material.

On February 5, 2013, we purchased the propane operating assets of Glades for approximately $2.9 million. The purchased assets are used to provide propane distribution service to approximately 3,000 residential and commercial customers in Okeechobee, Glades and Hendry Counties, Florida. In connection with this acquisition, we recorded $1.6 million in property, plant and equipment, $231,000 in propane and other inventory, $300,000 in an intangible asset related to Glades' customer list, to be amortized over 12 years beginning in February 2013, and $724,000 in goodwill. All of the goodwill is expected to be deductible for income tax purposes. These amounts reflect an adjustment to the allocation of the purchase price during the first quarter of 2014 based on our final valuation, which decreased the value of propane inventory by $271,000 and increased goodwill by the same amount. The revenue and net income from this acquisition that were included in our condensed consolidated statement of income for the three and six months ended June 30, 2014 were not material.

4. Rates and Other Regulatory Activities

Our natural gas and electric distribution operations in Delaware, Maryland and Florida are subject to regulation by their respective PSC; Eastern Shore, our natural gas transmission subsidiary, is subject to regulation by the FERC; and Peninsula Pipeline, our intrastate pipeline subsidiary, is subject to regulation by the Florida PSC. Chesapeake's Florida natural gas distribution division and FPU's natural gas and electric distribution operations continue to be subject to regulation by the Florida PSC as separate entities.

Delaware

There were no rates and other regulatory activities in Delaware during the first six months of 2014.

Maryland

On March 24, 2014, Sandpiper filed a depreciation study with the Maryland PSC regarding the assets purchased in the ESG acquisition. This depreciation study was filed in accordance with the order dated May 29, 2013, which allowed Sandpiper to recommend the proper depreciation rates and accumulated depreciation associated with the acquired assets. Sandpiper recommended slightly lower depreciation rates to be applied prospectively and a reduction of $4.5 million in accumulated depreciation. On June 20, 2014, the Maryland PSC staff recommended lower depreciation rates than those recommended by Sandpiper and a reduction of $5.5 million in accumulated depreciation. The Office of People's Counsel also recommended lower depreciation rates and no adjustment to accumulated depreciation. The parties are currently discussing a potential settlement in advance of an evidentiary hearing in August 2014.

Florida

On April 28, 2014, FPU filed a base rate proceeding for its electric distribution operation. FPU requested interim rate relief of approximately $2.4 million and final rate relief of approximately $5.9 million. The interim rate relief requested is based on the twelve-month period ended September 30, 2013. At the July 10, 2014 Agenda Conference, the Florida PSC approved interim rate relief of approximately $2.2 million, as recommended by the Florida PSC staff. The interim rates are effective for meter readings on or after August 10, 2014. Any increase to our rates as a result of this interim rate relief may be subject to refund, depending on the outcome of the final rate relief request. The base rate proceeding hearing is currently scheduled for September 15-18, 2014. The revenue requirement will be determined at the Agenda Conference, currently scheduled for November 25, 2014, and final rates will be determined at the Agenda Conference, currently scheduled for December 16, 2014. Final rates are expected to be effective in January 2015.

On January 13, 2014, FPU's natural gas divisions and Chesapeake's Florida natural gas distribution division filed a consolidated natural gas depreciation study with the Florida PSC. We also filed for approval to establish a regulatory asset and related amortization to address the costs associated with the development of this study. Depending on the results of this proceeding, we may be required to change depreciation expense for our Florida natural gas distribution operations. The PSC agenda date for the depreciation study has not yet been set.

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On November 15, 2013, Chesapeake's Florida natural gas distribution division petitioned the Florida PSC for an extension to its surcharge to recover an additional $381,000 in estimated remaining environmental cleanup costs that have not yet been recovered. This extension would be effective for two years, beginning January 1, 2014. The Florida PSC approved the extension of the surcharge and the additional amount for recovery at the Agenda Conference on January 7, 2014.

Eastern Shore

The following are regulatory activities involving FERC orders applicable to Eastern Shore and the expansions of Eastern Shore's transmission system:

TETLP Expansion Project: On January 31, 2014, Eastern Shore submitted to the FERC a request for prior notice authorization regarding a project that included certain improvements at Eastern Shore's existing interconnection with TETLP near Honey Brook, Pennsylvania. This project will allow Eastern Shore to increase its capacity to receive natural gas from TETLP by 57,000 Dts/d to a total capacity of 107,000 Dts/d, but this requested improvement will not result in an increase in Eastern Shore's overall system capacity. On April 8, 2014, the FERC approved Eastern Shore's prior notice application, and Eastern Shore made this additional receipt point capacity available to an existing industrial customer.

White Oak Lateral Project Filing: On June 13, 2013, Eastern Shore submitted to the FERC an application for a CP, seeking authorization to construct the White Oak lateral project located in Kent County, Delaware. The project consists of installing approximately 5.5 miles of 16-inch diameter pipeline, metering facilities and miscellaneous appurtenances, extending from Eastern Shore's mainline system near its North Dover City Gate Station to the Garrison Oak Technical Park, all located in Dover, Delaware. This project is designed to provide 55,200 Dts/d of delivery lateral firm transportation service to an industrial customer facility currently under construction. The total cost of the project is estimated to be approximately $11.5 million.

On August 9, 2013, the FERC issued a notice of intent to prepare an environmental assessment for the project. The comment period concluded on September 9, 2013, with no comments being filed in the docket. The environmental assessment was issued on October 4, 2013, and FERC staff recommended a finding of no significant impact. Eastern Shore filed the implementation plan and acceptance of conditions, stating that it will comply with all environmental conditions as set forth in the order. On November 27, 2013, the FERC issued a CP for this project. On January 17, 2014, the FERC issued its notice to allow construction to proceed, and Eastern Shore began construction activities for this project on January 22, 2014, for a planned in-service date of January 1, 2015.

Other matters: Eastern Shore also had developments in the following FERC matters:

On May 30, 2014, Eastern Shore submitted to the FERC a combined filing of its FRP and Cash-Out Refund for a twelve-month period from April 2013 to March 2014. In this filing, Eastern Shore proposed an FRP rate of 0.62 percent. During the period, Eastern Shore experienced an under-recovery of $494,000 in its Deferred Gas Required for Operations costs and an over-recovery of $160,000 in its Deferred Cash-Out costs. Eastern Shore proposed to incorporate the Cash-Out Refund into its FRP to mitigate the effect of the increase in the FRP to its customers.

5. Environmental Commitments and Contingencies

We are subject to federal, state and local laws and regulations governing environmental quality and pollution control. These laws and regulations require us to remove or remediate at current and former operating sites the effect on the environment of the disposal or release of specified substances.

We have participated in the investigation and assessment of, and have remediation exposures at, six former MGP sites. Those sites are located in Salisbury, Maryland, and Winter Haven, Key West, Pensacola, Sanford and West

Palm Beach, Florida. We have also been in discussions with the MDE regarding a seventh former MGP site located in Cambridge, Maryland. We were notified in December of 2013 by the DNREC that it would be conducting a facility evaluation of an eighth former MGP site located in Seaford, Delaware.

As of June 30, 2014, we had approximately $10.2 million in environmental liabilities related to all of FPU’s MGP sites in Florida, which include the Key West, Pensacola, Sanford and West Palm Beach sites, representing our estimate of the future costs associated with those sites. FPU has approval to recover up to $14.0 million of its environmental costs related to all of its MGP sites from insurance and from customers through rates, approximately $9.4 million of which has been recovered as of June 30, 2014. We had approximately $4.6 million in regulatory assets for future recovery of environmental costs from FPU’s customers.

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In addition to the FPU MGP sites, we had $454,000 in environmental liabilities at June 30, 2014, related to Chesapeake's MGP sites in Maryland and Florida, representing our estimate of future costs associated with these sites. As of June 30, 2014, we had approximately $503,000 in regulatory and other assets for future recovery through Chesapeake's rates. Environmental liabilities for all of our MGP sites are recorded on an undiscounted basis based on the estimate of future costs provided by independent consultants.

We continue to expect that all costs related to environmental remediation and related activities will be recoverable from customers through rates.

The following discussion provides details on MGP sites:

West Palm Beach, Florida

Remedial options are being evaluated to respond to environmental impacts to soil and groundwater at, and in the immediate vicinity of, a parcel of property owned by FPU in West Palm Beach, Florida, where FPU previously operated a MGP. FPU is currently implementing a remedial plan approved by the FDEP for the east parcel of the West Palm Beach site, which includes installation of monitoring test wells, sparging of air into the groundwater system and extraction of vapors from the subsurface. It is anticipated that similar remedial actions ultimately will be implemented for other portions of the site. Estimated costs of remediation for the West Palm Beach site range from approximately $4.5 million to $15.4 million, including costs associated with the relocation of FPU's operations at this site, which is necessary to implement the remedial plan, and any potential costs associated with future redevelopment of the properties.

Sanford, Florida

FPU is the current owner of property in Sanford, Florida, which was a former MGP site that was operated by several other entities before FPU acquired the property. FPU was never an owner or an operator of the MGP. In January 2007, FPU and the Sanford Group signed a Third Participation Agreement, which provides for the funding of the final remedy approved by the EPA for the site. FPU's share of remediation costs under the Third Participation Agreement is set at five percent of a maximum of $13.0 million, or $650,000. As of June 30, 2014, FPU has paid $650,000 to the Sanford Group escrow account for its entire share of the funding requirements.

The total cost of the final remedy is now estimated to be over $20.0 million, which includes long-term monitoring and the settlement of claims asserted by two adjacent property owners to resolve damages that the property owners allege they have incurred and will incur as a result of the implementation of the EPA-approved remediation. In settlement of these claims, members of the Sanford Group, which in this instance does not include FPU, have agreed to pay specified sums of money to the parties. FPU has refused to participate in the funding of the third-party settlement agreements based on its contention that it did not contribute to the release of hazardous substances at the site giving rise to the third-party claims. FPU has advised the other members of the Sanford Group that it is unwilling at this time to agree to pay any sum in excess of the $650,000 committed by FPU in the Third Participation Agreement.

As of June 30, 2014, FPU's remaining remediation expenses, including attorneys' fees and costs, are estimated to be $24,000. However, we are unable to determine, to a reasonable degree of certainty, whether the other members of the Sanford Group will accept FPU's asserted defense to liability for costs exceeding $13.0 million to implement the final remedy for this site, as provided in the Third Participation Agreement, or will pursue a claim against FPU for a sum in excess of the $650,000 that FPU has paid under the Third Participation Agreement. No such claims have been made as of June 30, 2014.

Key West, Florida

FPU formerly owned and operated a MGP in Key West, Florida. Field investigations performed in the 1990s identified limited environmental impacts at the site, which is currently owned by an unrelated third party. In 2010, after 17 years of regulatory inactivity, FDEP observed that some soil and groundwater standards were exceeded and requested implementation of additional soil and groundwater fieldwork. The scope of work is limited to the installation of two additional monitoring wells and periodic monitoring of the new and existing wells. The two new monitoring wells were installed in November 2011, and groundwater monitoring began in December 2011. The first semi-annual report from the monitoring program was issued in May 2012. The data from the June 2012 and September 2012 monitoring events were submitted to the FDEP on October 4, 2012. FDEP responded via e-mail on

October 9, 2012 that, based on the data, NAM appears to be an appropriate remedy for the site.
The FDEP issued a Remedial Action Plan approval order, dated October 12, 2012, which specified that a limited semi-annual monitoring program is to be conducted. The most recent groundwater-monitoring event was conducted on March

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13, 2014. The results were reported in a letter to FDEP dated April 26, 2014. Natural Attenuation Default Criteria were met at all locations sampled. The next semi-annual sampling event is scheduled for September of 2014. Although the duration of the FDEP-required limited NAM cannot be determined with certainty, it is anticipated that total costs to complete the remedial action will not exceed $50,000. The annual cost to conduct the limited NAM program is not expected to exceed $8,000.

Pensacola, Florida

FPU formerly owned and operated a MGP in Pensacola, Florida, which was subsequently owned by Gulf Power. Portions of the site are now owned by the City of Pensacola and the FDOT. In October 2009, FDEP informed Gulf Power that FDEP would approve a conditional No Further Action determination for the site, which must include a requirement for institutional and engineering controls. On December 13, 2011, Gulf Power, the City of Pensacola, FDOT and FPU submitted to FDEP a draft covenant for institutional and engineering controls for the site. Upon FDEP's approval and the subsequent recording of the institutional and engineering controls, no further work is expected to be required of the parties. Assuming FDEP approves the draft institutional and engineering controls, it is anticipated that FPU's share of remaining legal and cleanup costs will not exceed $5,000.

Winter Haven, Florida

The Winter Haven site is located on the eastern shoreline of Lake Shipp, in Winter Haven, Florida. Pursuant to a consent order entered into with FDEP, we are obligated to assess and remediate environmental impacts at this former MGP site. Recent groundwater sampling results show a continuing reduction in contaminant concentrations from the treatment system, which has been in operation since 2002. Currently, we predict that remedial action objectives could be met in approximately two to three years for the area being treated by the remediation system. On August 7, 2012, FDEP issued a letter discussing the need to evaluate further remedial options, which could incorporate risk-management options, including natural attenuation and the use of institutional and engineering controls. Modifications to the existing consent order and the remedial action plan modification could be required to incorporate risk-management options into the remedy for the site. A response letter was submitted to FDEP on May 7, 2013. FDEP issued an additional comment letter, dated September 16, 2013, containing various requests and questions, which we responded to on October 10, 2013.

An exploratory drilling program was conducted in November of 2013. The most recent groundwater monitoring event was conducted on April 11, 2014, and results were reported in a letter to FDEP dated June 6, 2014. A meeting was held with FDEP on June 12, 2014 to discuss the results of the drilling program, the groundwater conditions, and potential future remedial actions. FDEP indicated that it may be possible to close out the site with institutional controls without modifying the existing consent order. FDEP is currently evaluating its administrative options.

Even if modifications to the existing consent order and remedial action plan are required, we estimate that future remediation costs for the subsurface soils and groundwater at the site should not exceed $443,000, which includes an estimate of $100,000 to implement additional actions, such as institutional controls, at the site. If we are required to incur this cost, we continue to believe that the entire amount will be recoverable from customers through rates.

FDEP previously indicated that we could also be required to remediate sediments along the shoreline of Lake Shipp, immediately west of the site. Based on studies performed to date, and our recent meeting with FDEP, we believe that corrective measures for lake sediments are not warranted and will not be required by FDEP. We therefore have not recorded a liability for sediment remediation.

Salisbury, Maryland

We have substantially completed remediation of a site in Salisbury, Maryland, where it was determined that a former MGP caused localized groundwater contamination. In February 2002, the MDE granted permission to permanently decommission the systems used for remediation and to discontinue all on-site and off-site well monitoring, except for one well, which is being maintained for periodic product monitoring and recovery. We anticipate that the remaining costs of the one remaining monitoring well will not exceed $5,000 annually. We cannot predict at this time when the MDE will grant permission to permanently decommission the one remaining monitoring well.

Other

We are in discussions with the MDE regarding a former MGP site located in Cambridge, Maryland. The outcome of this matter cannot be determined at this time; therefore, we have not recorded an environmental liability for this location.

In a letter dated December 5, 2013, the DNREC notified us that it will be conducting a facility evaluation of a former MGP site in Seaford, Delaware. The facility evaluation has not been conducted, and the outcome of this evaluation cannot be determined at this time; therefore, we have not recorded an environmental liability for this location.

6. Other Commitments and Contingencies

Natural Gas, Electric and Propane Supply

Our natural gas, electric and propane distribution operations have entered into contractual commitments to purchase gas, electricity and propane from various suppliers. The contracts have various expiration dates. For our Delaware and Maryland natural gas distribution divisions, we have a contract, which expires on March 31, 2015, with an unaffiliated energy marketing and risk management company to manage a portion of the divisions' natural gas transportation and storage capacity.

In May 2013, Sandpiper entered into a capacity, supply and operating agreement with EGWIC to purchase propane over a six-year term. Sandpiper's current annual commitment is estimated at approximately 6.5 million gallons. Sandpiper has the option to enter into either a fixed per-gallon price for some or all of the propane purchases or a market-based price utilizing one of two local propane pricing indices.

Chesapeake’s Florida natural gas distribution division has firm transportation service contracts with FGT and Gulfstream. Pursuant to a capacity release program approved by the 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.

In May 2014, PESCO renewed contracts to purchase natural gas from various suppliers. These contracts expire in May 2015.

FPU’s electric fuel supply contracts require FPU to maintain an acceptable standard of creditworthiness based on specific financial ratios. FPU’s agreement with JEA requires FPU to comply with the following ratios based on the results of the prior 12 months: (a) total liabilities to tangible net worth less than 3.75 times, and (b) a fixed charge coverage ratio greater than 1.5 times. If either ratio is not met by FPU, it has 30 days to cure the default or provide an irrevocable letter of credit if the default is not cured. FPU’s electric fuel supply agreement with Gulf Power requires FPU to meet the following ratios based on the average of the prior six quarters: (a) funds from operations interest coverage ratio (minimum of 2 times), and (b) total debt to total capital (maximum of 65 percent). If FPU fails to meet the requirements, it has to provide the supplier a written explanation of actions taken or proposed to be taken to become compliant. Failure to comply with the ratios specified in the Gulf Power agreement could result in FPU having to provide an irrevocable letter of credit. As of June 30, 2014, FPU was in compliance with all of the requirements of its fuel supply contracts.

Sharp entered into a separate supply and operating agreement with EGWIC. Under this agreement, Sharp has a commitment to supply propane to EGWIC over a six-year term. Sharp's current annual commitment is estimated at approximately 6.5 million gallons. The agreement between Sharp and EGWIC is separate from the agreement between Sandpiper and EGWIC, and neither agreement permits the parties to set off the rights and obligations specified in one against those specified in the other.

Corporate Guarantees

The Board of Directors has authorized us to issue corporate guarantees securing obligations of our subsidiaries and to obtain letters of credit securing our obligations, including the obligations of our subsidiaries. The maximum authorized liability under such guarantees and letters of credit is $45.0 million.

We have issued corporate guarantees to certain vendors of our subsidiaries, the largest portion of which is for Xeron and PESCO. These corporate guarantees provide for the payment of propane and natural gas purchases in the event of the respective subsidiary’s default. Neither subsidiary has ever defaulted on its obligations to pay its suppliers. The liabilities for these purchases are recorded when incurred. The aggregate amount guaranteed at June 30, 2014 was $31.6 million, with the guarantees expiring on various dates through June 2015.

Chesapeake guarantees the payment of FPU’s first mortgage bonds. The maximum exposure under the guarantee is the outstanding principal plus accrued interest balances. The outstanding principal balances of FPU’s first mortgage bonds approximate their carrying values (see Note 14, Long-Term Debt, to the condensed consolidated financial statements for further details).

In addition to the corporate guarantees, we have issued a letter of credit for $1.0 million, which expires on September 12, 2014, related to the electric transmission services for FPU's northwest electric division. We have also issued a letter of credit to our current primary insurance company for $1.1 million, which expires on December 2, 2014, as security to

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satisfy the deductibles under our various insurance policies. As a result of a change in our primary insurance company in 2010, we renewed and decreased the letter of credit for $304,000 to our former primary insurance company, which will expire on June 1, 2015. There have been no draws on these letters of credit as of June 30, 2014. We do not anticipate that the letters of credit will be drawn upon by the counterparties, and we expect that the letters of credit will be renewed to the extent necessary in the future.

We provided a letter of credit for $2.3 million to TETLP related to the precedent agreement and firm transportation service agreement between our Delaware and Maryland divisions.

On July 25, 2014, we provided a letter to the Florida PSC guaranteeing potential refunds from interim rates to be charged by our Florida electric operation. The interim rates, which provide a rate relief of approximately $2.2 million of revenue on an annual basis, were approved by the Florida PSC in July 2014 in connection with the base rate proceeding currently in progress. This guarantee will expire upon the release by the Florida PSC at the conclusion of the base rate proceeding. See Note 4, Rates and Other Regulatory Activities, for further details on the base rate proceeding involving the Florida electric operation.

Tax-related Contingencies

We are subject to various audits and reviews by the federal, state, local and other regulatory authorities regarding income taxes and taxes other than income. As of June 30, 2014, we maintained a liability of $300,000 related to unrecognized income tax benefits and $905,000 related to contingencies for taxes other than income. As of December 31, 2013, we maintained a liability of $300,000 related to unrecognized income tax benefits and $1.0 million related to contingencies for taxes other than income.

Other

We are involved in certain other legal actions and claims arising in the normal course of business. We are also involved in certain legal and administrative proceedings before various governmental agencies concerning rates. In the opinion of management, the ultimate disposition of these proceedings will not have a material effect on our consolidated financial position, results of operations or cash flows.

7. Segment Information

We use the management approach to identify operating segments. We organize our business around differences in regulatory environment and/or products or services, and the operating results of each segment are regularly reviewed by the chief operating decision maker (our Chief Executive Officer) in order to make decisions about resources and to assess performance. The segments are evaluated based on their pre-tax operating income. Our operations comprise three operating segments:

- Regulated Energy. The Regulated Energy segment includes natural gas distribution, natural gas transmission operations and electric distribution operations. All operations in this segment are regulated, as to their rates and services, by the PSC having jurisdiction in each operating territory or by the FERC in the case of Eastern Shore.
- Unregulated Energy. The Unregulated Energy segment includes propane distribution and wholesale marketing operations, and natural gas marketing operations, which are unregulated as to their rates and services. Also included in this segment are other unregulated energy services, such as energy-related merchandise sales and heating, ventilation and air conditioning, plumbing and electrical services.
- Other. The “Other” segment consists primarily of our advanced information services subsidiary, as well as our unregulated subsidiaries that own real estate leased to Chesapeake and certain corporate costs not allocated to other operations.

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The following table presents financial information about our reportable segments:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
(in thousands)				
Operating Revenues, Unaffiliated Customers				
Regulated Energy	$61,348	$54,975	$163,222	$136,279
Unregulated Energy	34,299	34,273	114,173	89,264
Other	4,850	4,898	9,439	9,331
Total operating revenues, unaffiliated customers	$100,497	$94,146	$286,834	$234,874
Intersegment Revenues (1)				
Regulated Energy	$298	$241	$590	$504
Unregulated Energy	22			