

**BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI**

In the Matter of the Application of Southern Missouri)	
Gas Company, L.P., d/b/a Southern Missouri Natural)	
Gas, for a Certificate of Public Convenience and)	
Necessity Authorizing it to Construct, Install, Own,)	<u>Case No. GA-2007-0212</u>
Operate, Control, Manage and Maintain a Natural Gas)	et al.
Distribution System to Provide Gas Service in)	
Lebanon, Missouri.)	

**BRIEF OF INTERVENOR
MISSOURI PROPANE GAS ASSOCIATION**

Three applications by Southern Missouri Natural Gas (“SMNG”) are combined into this one consolidated case. First is an application for a certificate of convenience and necessity to construct, operate and maintain a natural gas distribution system and provide gas service in Lebanon, Missouri (GA-2007-0212, the lead case). There is a similar application for a certificate of convenience and necessity to provide natural gas service in Houston and Licking (GA-2007-0310). Finally SMNG applies for authority to finance the expansions of service into those three cities. (GA-2007-0215). Missouri Propane Gas Association (“MPGA”) sought and was granted intervention in the Lebanon case. SMNG requested a hearing in the consolidated cases, which took place on July 27, 2007. For the reasons discussed herein, the Commission cannot grant SMNG's requests.

A. SMNG’s Application Cannot be Granted Until it Complies with the Filing Requirements of 4 CSR 240-3.205

As a preliminary matter, the Commission may not grant the Lebanon application until SMNG provides the information required by regulation. A gas utility applicant requesting a certificate of convenience and necessity from the Commission must include various statements or items in its application. 4 CSR 240-3.205. The regulation states that if any of the items required under the rule are unavailable at the time the application is filed, “they shall be

furnished prior to the granting of the authority sought.” 4 CSR 240-3.205(2). In this case, SMNG has not provided the information required by the regulations. SMNG has not provided a ½” per mile plat map comparable to county highway maps issued by MODOT or a plat map at a scale of 2,000 feet/inch. The only “map” that Applicant Southern Missouri Natural Gas (“SMNG”) submits is no where close to a county highway map and has no indication of what scale it is, if any. Exhibit 2, Appendix B, Maps of Proposed Service Area; Tr.¹ 258:15-23, 267:3-12. Nor has SMNG provided a valid city franchise for Lebanon. As discussed in the staff recommendation, the franchise SMNG entered into with the City of Lebanon is not valid because it violates previous orders of the PSC. SMNG has failed to meet the requirement of the regulations which have the force and effect of law. Missouri Nat’l Educ. Ass’n v. Missouri State Bd. of Mediation, 695 S.W.2d 894, 897 (Mo banc 1985). This Commission must adhere to its own regulations. Id. A certificate cannot be granted until SMNG complies with the requirements.

B. Standards for Granting a Certificate of Convenience and Necessity

The expansion requests into the three cities are governed by prior Commission decisions. The applicant must meet five standards to obtain a certificate of convenience and necessity. The standards required for issuing a certificate are:

- (1) There must be a need for the service;
- (2) The applicant must be qualified to provide the proposed service;
- (3) The applicant must have the financial ability to provide the service;
- (4) The applicant’s proposal must be economically feasible; and
- (5) The service must promote the public interest.

¹ All references to the transcript are to Volume II, the transcript of the evidentiary hearing held on July 27, 2007.

In re Empire District Electric Co. 8 Mo. P.S.C. 3d 426, ____ (1999)(citing In re Ozark Natural Gas Co., 5 Mo. P.S.C. 3d 143, 146 (1996); In re Tartan Energy Co., 3 Mo. P.S.C. 3d 173, 177 (1994); and In re Intercon Gas, Inc., 30 Mo. P.S.C. (N.S.) 554, 561 (1991)).

For each element, the burden of proof “rests firmly upon the applicant.” State ex rel. Oliver v. Public Service Comm’n, 524 S.W.2d 595, 598 (Mo.App. 1976). “Each element is essential. Absence of even one of the five elements should result in denial of the application.” In re Osage Water Co., 8 Mo. P.S.C.3d 366, ____ (1999)(Comm’r Murray, dissenting). In this case, SMNG has simply not met its burden and denial of the application is appropriate.

1. SMNG Failed to Present Evidence of Need.

SMNG has failed to meet its burden of establishing need. Although SMNG presented testimony that some may desire natural gas, SMNG failed to present evidence of any need at all. To the contrary, the evidence presented showed that Lebanon has seven providers of propane within the city, and five or six more that come into Lebanon. Tr. 206:9-14. Lebanon also has electricity, which is provided by the City. Tr. 181:22-24. The only testimony offered by SMNG was that certain City officials want natural gas, but there is no evidence of need. Even that testimony failed to provide substantial evidence of even desire. City officials related hearsay concerning three potential businesses that might have wanted natural gas, but there was no evidence concerning a need for natural gas. Tr. 181:1-6.

The recent vote in Lebanon, which is in the record, also indicates the lack of a need for the service. SMNG’s own studies (based on public census information) indicate that there are over *****Proprietary***** households in Lebanon. Exhibit 4P. Yet, when asked to vote on the issue of whether to provide a franchise, only 948 people chose to vote and of those only 602 voted for the proposal. Using an estimate of two votes per household, it is clear that only about 300 households may have a desire for natural gas as an option. The remaining households in

Lebanon are not concerned enough with the issue to even vote. There is no logical way the vote can be taken as evidence of need.

2. SMNG is not qualified to provide the proposed service.

Although the system that SMNG currently operates has been in existence since approximately 1995 (Exhibit 1), the current ownership of the system has been in place only since 2005 (Tr. 42:20). SMNG currently has a relatively small customer base of approximately 7,500 customers, with approximately 6,800 of those being residential. Tr. 70:16-18. SMNG's qualifications can only be based on a two year track record with an existing customer base. SMNG's lack of compliance with PSC regulations and its financial track record indicate that it should not be granted an additional monopoly. As will be addressed in other standards, below, SMNG has not established that it has the financial ability to provide the service nor has it met its burden of demonstrating economic feasibility. Accordingly, a look at SMNG's financial-related qualifications and its structure are extremely important considerations.

SMNG is the d/b/a for Southern Missouri Gas Company, LP, which has no parent or guarantor. SMGC LP is comprised of a 2% general partnership interest by Sendero SMGC GP Acquisition Co., LLC and a 98% limited partnership interest by Sendero SMGC Limited Acquisition Co., LLC. Exhibit 10; Accord Tr. 77:4-8. These two limited liability companies are, in turn, owned by Sendero Capital Partners Missouri, LLC (4.559%), CHx Capital Missouri, Inc. (93.0639%) and Michael J. Lewis (2.3771%). Id. Sendero Capital Partners Missouri, LLC is owned 100% by Randal Maffett. Tr. 131:4-9. CHx Capital Missouri, Inc. is owned 100% by Alex Cranberg. Tr. 131:17-19.

The two Sendero SMNG entities have no other assets other than their interests in SMNG. Id.; Tr. 77:9-24, 78:15-24. All of SMNG's financings were secured by assets of SMNG; there is no recourse to any other entity. Id. SMNG has a management contract with Sendero Asset

Management, LLC for approximately \$200,000 per year. Tr. 77:25-78:9. SMNG presented no evidence concerning the track records of these companies because there is none to present.

These companies exist solely for the purpose of running and profiting from SMNG.

a. The Ownership Structure of SMNG is in Flux

Randal Maffett testified that he is one of the owners and the primary managing partner of SMNG. Tr. 41:20-23. Mr. Maffett is also the president and CEO of Sendero Asset Management, LLC. Tr. 41:24-42:1. SMNG is seeking authority for an additional \$10 Million in equity investment. Exhibit 7. Mr. Maffett testified that the ownership structure as set forth above (and in Exhibit 10) would change with the financing that is the subject of this consolidated case. Tr. 134:5-135:19. It is anticipated that the current ownership of the Sendero GP and LP LLCs would shift, diluting the interests of Sendero Capital Partners Missouri, CHx Capital Missouri and Mr. Lewis. Id. But Mr. Maffett cannot predict that this will be the case as it depends on the desires of the potential equity investors. Id. There was no testimony about whether the equity injection might change the control and operations of SMNG. Without details of the demands tied to either the proposed equity injection or the proposed debt to be incurred, it seems that who will be running SMNG and what limitations will be placed on how it is run are unknown. Id.; Tr. 295:3-17. As such, SMNG has failed to meet its burden of establishing that the management and ownership have the ability to provide the service.

b. Current Management's Track Record is Poor

Even if the control stays the same, SMNG, since the acquisition by Sendero, has encountered significant problems. In the first two years, Sendero had to reinvest approximately 1.5 Million back into the company. Tr. 137:22-138:2. And the ownership has not taken any dividends or distributions out of the company. Tr. 138:2-5. Although Mr. Maffett at first testified to this fact as if it was done out of some altruistic commitment to the customers (Tr.

137:25-138:5), staff testimony revealed that GMAC, the current creditor, prohibited SMNG's owners from taking any distributions during its first three years, apparently because GMAC was concerned about the way the company was being managed (Tr. 295:8-12).

Natural gas companies need adequate amounts of working capital because of the delay in recovering payments from the consumers. Tr. 150:17-151:2; 295:18-297:4. But SMNG has failed to plan for this fundamental business factor and at one point ran out of working capital, requiring an infusion of \$400,000 from Alex Cranberg. 295:18-297:4. SMNG was forced to renegotiate its working capital line of credit with GMAC from 1.5 Million to 3.5 Million. Id. Part of the \$50 Million in debt SMNG is seeking approval for is a line of \$25 Million for working capital. Exhibit 8P; Tr. 296:15-21. PSC Staff is considering whether the amount is more than is needed. Tr. 296:15-21. SMNG management is does not appear to be capable of planning for business contingencies and certainly fails to meet its burden in this regard.

Nor has SMNG complied with Commission requirements concerning business operations. In October 2005, the Office of Public Counsel (OPC) filed a complaint before the Commission (GC-2006-0180) alleging SMNG was not following 4 CSR 240-40.018 regarding diversification to mitigate volatility and secure adequate supplies. See Tr. 145:24-146:21. The result of the case was an April 2006 stipulation that required hedging for winter use in certain percentages by certain dates. Id. SMNG was not properly mitigating volatility until forced to do so by the OPC, another indication that it is not capable of providing the service.

Tied into all this is SMNG's increase in its Purchased Gas Adjustment ("PGA") rate. Mr. Maffett explains it as having been due to, after the hurricanes, paying \$12 for gas but selling it at \$7 under the previous tariff sheet. Tr. 151:3-10. This, in combination with the float between paying for gas and recovering costs from the consumer being 40 days or more, caused concerns

about cash flow for SMNG, especially in light of the stipulation (above) that it would hedge more. Tr. 150:3-13.

Additional concerns about SMNG's financial stability are found in a currently-pending case (GR-2006-0352) where, after conducting an audit of SMNG's 2005-2006 Actual Cost Adjustment ("ACA") filing, staff is recommending that between \$220,450 and \$378,470 in costs essentially be disallowed. Exhibit 11. The PSC Staff is making the adjustment recommendation based upon the (inadequate) hedging practices of SMNG going into the winter of 2005/2006. Id. PSC Staff also recommended that SMNG further diversify its gas supply portfolios including a gas supply planning horizon of multiple years. Exhibit 11. SMNG concurs with these recommendations. Id. This case is still pending. Again, an indication that SMNG has not engaged in sound business practices.

But most damaging to SMNG's burden of establishing that they can provide the service, is SMNG's response to the above recommendation. In its response to the PSC Staff recommendation, SMNG stated that a disallowance of as little as \$220,450 "would be financially detrimental to the Company's ability to continue to provide safe and reliable service throughout its Missouri service areas." Id.; Tr. 86:22-12. SMNG has admitted in filings before this Commission that its margin for error is so tight that "safe and reliable service" would be jeopardized if as little as \$220,450 in adjustments was made. Either SMNG's representation in the other case is correct, in which case this Commission should not grant an additional service area when SMNG cannot provide safe and reliable service to its current service area or SMNG has blatantly misrepresented its position to the Commission in an attempt to avoid compliance. Either way, SMNG's position concerning the ACA should by itself lead to a denial of a certificate for an additional service area.

In sum, among the qualifications to look at regarding an applicant for CCN is financial management abilities and business planning abilities. See Tr. 254:19-22. Financial ability to pay for the project is a separately identified standard – whether the money exists to fund the expansion. And economic feasibility is an issue as well – whether the project looks like it will work based on the projections. But surely this Commission does not only regard having money and a plan to make some money as being enough. The qualifications of the applicant with regard to its demonstrated abilities (or lack thereof) to manage a company well must also be considered. This is where SMNG falters. The current SMNG had been operating for about a year and a half when it applied for this expansion. As noted above, it has already been shown to have problems with hedging, gas supply planning and maintaining adequate amounts of working capital. Its current creditor won't let distributions be made. An exchange between Commissioner Gaw and PSC staff member Dave Murray about the financial condition of the company expresses the concern very aptly:

Q. [by Comm'r Gaw] That -- the very basic premise that you were discussing in regard to the current credit rating of this company, or where you think it lies, how much concern does Staff have if that -- with what you told me about the credit rating and its comparability to another utility about allowing any kind of an expansion until that credit rating improves?

A. [by Mr. Murray] It is a big concern, and that's why I am really wanting to see the final terms and conditions of what these investors are -- you know, what they see and, you know, how much -- you know, how much restriction are they going to put on Southern Missouri Natural Gas with its use of funds. GMAC, who is the current creditor, has -- I know Randy indicated they haven't received any distributions. But GMAC said,

you're not going to take any distributions for three years. And so I would be interested to see what -- you know, what type of restrictions are they going to put on this company going forward to ensure that they don't just let this, you know, company do whatever it wants.

Tr. 294:21-295:17. So PSC Staff has a big concern about allowing the expansion SMNG has requested given its financial health. PSC Staff also testified that even with the proposed equity injection, the financial health of SMNG is uncertain. Tr. 298:11-20. These concerns are well-justified and SMNG has failed to meet its burden to overcome them.

PSC Staff also expressed concerns about the valuation of SMNG having been done under one method when Sendero acquired SMNG but appearing to be valued differently in current audited financial statements. Exhibit 19; Tr. 274:24-279:14. The reason PSC Staff view this issue as important is that they want to ensure that the investment opportunity has been fairly represented to the proposed equity investors. Exhibit 19. As PSC staff testified:

A. [by Mr. Murray] Oh, it's important because I want to know what the investors -
- how they're looking at it. I want to make sure that they are looking at the economics of this proposal, of the existing Southern Missouri Natural Gas properties and the proposed expansion. I just want to make sure that they don't feel like that there is this much equity based on the \$45 million historical cost. I want to make sure they don't think that there's that much equity in this property. I just -- I don't believe that that's the case.

Tr. 278:20-279:5.

In light of its financial condition, Mr. Maffett's responses to questions about break-even points or minimum conversion requirements are especially troubling. SMNG has not truly planned for this expansion in the way that one expects a business to plan. When Mr. Maffett was

asked by Commissioner Clayton how many customers SMNG needed to sign up for service to make the project successful, he replied that they did not look at that. The exchange:

Q. [by Comm'r Clayton] Well, in this -- I guess what I'm trying to ask is, in this business, which is where you're going to have build out -- you're going to have a capital investment --

A. [by Mr. Maffett] Right.

Q. -- to actually get the product to people's houses, how many customers do you need to sign up before you call this a success?

A. I mean, we just didn't analyze it that way, because we took a ten-year approach. I can --

Q. So does that --

A. -- make an estimate.

Q. -- mean we have to wait ten years to determine whether or not this was a worthwhile --

A. No, sir.

Q. -- endeavor?

A. No, sir. The definition of success in my book is the opportunity to earn the regulated return that you approve. And it would take me, as according -- this is the -- kind of the realistic plan using can back off. And I believe Staff has a witness who will testify to the sensitivity analysis that they did on our customer counts that will demonstrate that there's -- there is a lot -- there is a lot of opportunity for lower-level growth and still having a feasible project. But we've tried to use realistic data, not pro forma or projected data.

Q. Well, I understand that. I'm trying to get a sense of after one year and you're off your projections, is the -- I don't want to say the project is in jeopardy. I mean, that's almost too dramatic. I'm just saying, at what -- are your targets set up to -- in a way that you need to make those targets to meet a certain level of revenue for the venture to be a success up to that point? Or is it just not set up that way. It doesn't make any sense.

A. It's -- our analysis isn't set up that way.

Tr. 152:6-153:18.

An exchange between Commissioner Gaw and Mr. Maffett reveals SMNG's "planning" on this business issue:

Q. [by Comm'r Gaw] Okay. And the effect of that would be, if there is -- if for some reason the anticipation doesn't play out -- well, it doesn't play out like you anticipate, and the company doesn't financially make it, then what -- how does -- how are the ratepayers protected, in your understanding?

A. [by Mr. Maffett] I mean, I'm not an expert in the course of bankruptcy law or in the course of regulatory law.

Q. Yes.

A. But my understanding is, you know, you control and regulate the rates that we're allowed to recover. And if I go out and spend money and we can't successfully market our products and services --

Q. Yes.

A. -- that I have the right to come and ask for rate increases and you have the right to deny those rate increases. And that it's -- it would be on prudence and reviewed.

Tr. 136:22-137:14.

One can only conclude there is no make-or-break point because SMNG's plan is to just ask to charge the customers more. Failure, then, will be due to the Commission denying rate increases or disallowing costs. This not only shows an inadequate planning process, but it goes to who bears the risk of a failed project, which will be discussed separately under the economic feasibility standard. The above exchanges clearly demonstrate that SMNG does not have a "break even" plan.

As set forth in the PSC Staff Recommendation Memorandum, the language of the franchise agreements with the cities allows each city the option to purchase the distribution system for net book value plus 15%. Exhibit 19; see also Appendix D to Exhibit 5 and Appendix D to Exhibit 3. If any of the cities exercise the option, the stipulation and agreement in Commission Case No. GA-94-127 would be violated. Exhibit 19. The stipulation was that the predecessor of SMNG would only provide retail natural gas service. Id. SMNG has apparently promised the Cities something it knew or should have known it cannot deliver.

Another indication of SMNG's business practices is that what it advertises on its web site regarding conversion costs is in conflict with the tariff sheets. Exhibit 14; Tr. 35:10-17; 124:3-125:23; 155:7-156:3; 165:13-167:7. Luring potential customers in with a promise of free conversion but then in reality charging them for anything over \$250 (for residential) is not an honest business practice. SMNG's strategy is clearly to lure customers away from other energy providers with deceptive advertising. Any business built on such a strategy is doomed to failure and the Commission should consider this practice in considering whether SMNG is truly capable of providing the service.

The demonstrated history of this company under Sendero ownership and management, albeit short, must be considered as part of the qualifications analysis. This Commission should

not take a company with SMNG's issues and allow it to expand even more, putting even more at risk, for it, for the Commission, for the people they both serve. SMNG, under Sendero's ownership, must better demonstrate its abilities in the natural gas distribution business before the Commission allows it to expand even more.

3. The applicant must have the financial ability to provide the service.

SMNG admits that it cannot proceed with the expansion of service into Lebanon, Houston and Licking without approval of the financing request as well. Tr. 90:11-14. SMNG admits it has no commitments or even conditional commitments for financing. Tr. 91:12-22. The terms have been "notionally" discussed with the three "short listed" bidders. Tr. 134:1-2. Mr. Maffett testified that general term sheets with a lot of blanks in them were sent to potential investors. No definitive term sheets exist. Tr. 92:5-14. This leaves too many unknowns for the PSC staff, and they cannot recommend approval of the financing application without more information. Exhibit 19; Tr. 272:2-273:10; 281:16-282:4; 287:6-15.

The only reason articulated by Mr. Maffett for the Commission giving conditional approval of the CCNs pending acceptable financing is as follows:

Q. Mr. Maffett, would you explain the importance of receiving a conditional CCN as a part of your need to close with the financiers?

A. Yes, sir. It's primarily to demonstrate to the potential investors that not only is the market there and the market feasible, but that regulatory support is there for the expansions and supporting the growth of the company.

Tr. 67:12-19. But Mr. Maffett admitted that SMNG does not need a conditional CCN in order to obtain financing:

Q. Right. And you want the Commission, as I understood your testimony earlier, to give you a certificate so that you can obtain the financing?

A. We're asking the Commission to show its support for the expansion in order to close the financing.

Q. And I guess I just wasn't completely clear. Are you saying that you don't think you can get the financing without this Commission's expression of support, as you call it?

A. No. I did not say that. Those are your words.

Q. Well, can you get the financing without this Commission's expression of support?

A. It could be possible.

Tr. 90:20-91:9. There is no dispute that SMNG does not currently have the financial ability to provide the service. SMNG admits it was possible to obtain financing before the Commission rules on the CCN, yet SMNG chose to make its application without such financing in place – even on a conditional basis. SMNG offered no evidence that anyone is willing to provide financing for this project. As such, SMNG has utterly failed to meet its burden on this issue and its application must be denied.

4. The applicant's proposal must be economically feasible.

Many of the key factors to be considered under this standard have already been articulated under the qualifications standard. The Commission has stated that its role is not “to manage the business affairs and decisions of the investor-owned utilities which it regulates, so long as the ratepayers are protected from potential abuses by the monopoly provider.” In re Missouri Gas Company, 4 Mo. P.S.C. 3d 13, ___ (1995). However, “if a utility makes what would be, in an unregulated marketplace, poor business decisions and takes uneconomic actions based upon those decisions, the general body of ratepayers should not have to bear the financial burden associated with such uneconomic actions.” Id.

The instant case is one in which the ratepayers are the only ones who stand to lose if the plan does not work. This is not a case like the expansion case for Rolla, Missouri, in which this Commission determined that the size and strength of the parent company of the applicant helped make a difference in the feasibility analysis. In re Utilicorp United, Inc., d/b/a Missouri Public Service, 3 Mo. P.S.C.3d 127 (1994). Missouri Public Service (“MPS”) provided natural gas to 42,000 customers in the state at the time of the application. Utilicorp had various utility holdings throughout the United States and abroad, including MPS. Id. Utilicorp was investor owned and at the time had assets of approximately one billion dollars. Id. The size and diversity of Utilicorp and MPS were considered by the Commission to be a substantial advantage in the venture. Id. The Commission added that a smaller, financially marginal company would either not propose or not be given the opportunity to engage in such a project. Id.

The Commission revisited its analysis in Utilicorp a few years later. Empire District Electric Company applied for a CCN to expand its electric services into additional portions of Greene County (than what it already served). In re Empire District Electric Co., 8 Mo. P.S.C. 3d 426 (1999). The Commission’s purpose in requiring a showing of financial feasibility was articulated:

A utility’s customers and the public could be harmed if the utility jumped into a project that would be a financial drain on the company. In determining whether there is a financial risk, it is appropriate to examine the overall financial strength and stability of the company.

Id. (citing Utilicorp). In the Empire case, as with the Utilicorp case, the financial health of the applicant or its parent was significant. Empire had provided evidence that the construction costs for the expansion project amounted to .4% of its total construction budget. Empire. The

Commission concluded that the project was not going to put the financial health and stability of Empire at risk. Id.

The reasoning concerning Empire Electric and Utilicorp lead to the conclusion that SMNG's proposal rests on the backs of ratepayers. SMNG currently serves approximately 7,500 customers. Tr. 70:16-18. Its feasibility study projects adding ***Highly Confidential*** customers by expanding to Lebanon, Licking and Houston. Exhibit 6HC. That is a large increase for a small company. SMNG plans to use the same set of rates for all of the communities it serves – the current ones and the proposed Lebanon, Licking and Houston communities. Any problems therefore with the feasibility of this expansion, if it turns into a rate increase or ACA adjustment issue, will be borne by all customers. Tr. 65:1-11; 284:15-24. SMNG claims that if the project fails, the shareholders must bear the risk. Tr. 75:13-25. But shareholders with no other assets besides SMNG's assets cannot truly be said to bear such a risk. They have nothing at risk besides the company's assets. The situation with SMNG is a far, far cry from that with Empire Electric or Utilicorp. There is no parent company with additional assets to absorb the losses. While there is additional equity under the financing plan, there are also large amounts of debt to be incurred. And because the final terms and conditions of either the equity or debt financing are unknown, it is also unknown how low returns or defaults will be addresses. An equity investor acquiescing to a lower than expected rate of return is one thing. It is completely another if there is a bankruptcy or cessation of service. These are not cases where the ratepayers are saved from costs. To the contrary. The testimony of Mr. Murray in response to Commissioner Gaw's questions tells the story (emphasis added):

Q. Is it a concern for Staff -- back to my question -- as to how this acquisition and the financing that goes along with it may impact current customers of the company?

A. I -- it -- I don't have that concern from the standpoint of the rate-making issue, because we can control that. As I said, with Aquila, we've done that. But I am concerned -- and this is just because we just haven't had a dead body, if you will, on a bankruptcy. I think the closest we've got maybe is [Gallatin] and Hamilton, where they refuse to -- the lender that took over was supposedly refusing to provide natural gas for the upcoming winter months. And we got a buyer to come in, and thank God things worked out. But, you know, that's uncharted territory. I -- and I'm not a bankruptcy expert. I -- who knows. I mean, I'm not sure.

Q. Well, let's go through the possible scenarios, in hopefully not too much time here. When you're looking at the possibility of an expansion, if the expansion here caused there under the financing terms to be a -- there to be a need to raise rates in order to maintain the financial integrity of the company, is that potentially a detriment to the current ratepayers?

A. If we allow those increased costs to go through, yes, it is.

* * *

Q. Now, let's look at the alternative that you were talking about. Let's say that the Staff -- and perhaps the Commission agreed with them, if you were walking down that line of scenarios, that there would not be an allowance for that additional increase in rates because of the acquisition and the financing causing there to be a need for additional revenues. Let's say that occurred. Okay. Now, let's assume that because of that the company was forced into a bankruptcy situation. And I'm not saying that would happen here. I'm not suggesting that's the case that's going to happen. Under that scenario, is

there not another risk to the existing ratepayers, or a series of risks to the existing ratepayers?

A. I wish I could answer that, but I just don't know. I don't know what would happen because something like with [Gallatin] -- Hamilton and [Gallatin] where somebody purchased the property, even though they were getting ready to shut off the gas.

Q. Well, let's say that there was an inability to find anyone who would operate the system under those rates that had been approved by the Commission and the Commission refused -- had refused to approve higher ones. Let's assume that scenario. Would there be a detriment to the existing consumers of the company?

A. They would no longer have safe and reliable service. I don't know how you could come to any other conclusion.

Q. Okay. Now let's assume that -- another possibility, which again may not -- which may not be a legal possibility, but it's not impossible, either. Let's assume that the bankruptcy court that you're dealing with suggested that under these circumstances, they have superior authority over this Commission to ensure that the creditors have their adequate return under some sort of a system to resolve the case, and the rates will be raised. Would that be a detriment to the ratepayers in that event -- this acquisition with the financing that caused all of this?

A. If that cost -- if the rates put into place are higher than a reasonable cost of service, yes, I would say that would be a detriment.

Q. Okay. So all I'm trying to get to here is that the -- there is a significant importance in regard to what this financing arrangement may be. Correct?

A. Yes.

Q. And that financing arrangement is something that the staff needs to be able to fully evaluate before they can fully evaluate the public interest of this acquisition.

A. Of the -- or the certificate, yes.

Tr. 283:22-287:15.

Rather than save for another day the Hobson's choice between allowing rate increases or a potential bankruptcy and/or cessation of service, the Commission can take action now to prevent such a scenario by denying the CCNs to SMNG and require it to become a financially stable company before allowing it to expand its service areas.

5. The service must promote the public interest.

The public interest in this case is not served by granting SMNG a monopoly to provide service in Lebanon. To the contrary, many of the citizens of Lebanon will be negatively impacted if this Commission grants the application. Propane is not regulated in the sense that government regulates what it can charge for propane gas. This is because the infrastructure that leads to a monopoly is not present with propane gas suppliers. But one must be careful not to mistake a lack of regulation of cost for no controls over cost whatsoever. To the contrary, the good old American way of open market competition is what "regulates" propane gas prices. As already noted, the people of Lebanon have seven to 13 providers of propane gas to choose from. Tr. 206:9-14. Lebanon also has electricity, which is provided by the City. Tr. 181:22-24. So there is already one regulated monopoly and several unregulated competitive providers for heat and cooking heat for Lebanon. SMNG and natural gas will overcrowd the market, necessarily (and by plan) drawing from the users of electric and propane gas.

The purpose of the Commission has been well-articulated as far as allowing multiple providers in an area:

To secure to the public all advantages to be gained from competition in obtaining fair rates and good service and also to protect them from its disadvantages, the commission was given authority to regulate rates, to investigate complaints about service, to compel companies to adequately serve all persons and industries in the territory in which they operate, to order improvements and safety equipment, and to authorize the abandonment or extension of lines and the financing of all improvements or purchases. The question of whether regulated monopoly or regulated competition will best serve the public convenience and necessity in a particular area at any time is for the commission to decide ...

StopAquila.org v. Aquila, Inc, 180 S.W.3d 24, 35 (Mo.App. 2005)((quoting People's Tel. Exch. v. Pub. Serv. Comm'n, 186 S.W.2d 531, 538 (Mo.App. 1945)(quoting State ex rel. City of Sikeston v. Pub. Serv. Comm'n, 82 S.W.2d 105, 110 (Mo. 1935))). “Thus, the regulatory powers accorded the Commission ... ultimately answer to the public interest” StopAquila.org, 180 S.W.3d at 35.

SMNG’s goal is to convert 50% of residential propane gas users to natural gas over a five year period. Tr. 35:24-36:2; 96:21-97:1; see also Exhibit 4P. There is no conversion projection for office and industrial users, but it is clear that converting industrial users is extremely important to the success of the expansion. See Exhibit 4P; Tr. 98:1-11. So SMNG’s success relies on taking half the current residential propane users and an unspecified, but surely significant, portion of the industrial users of propane. This will doubtless have a negative effect on the propane industry and those it employs. Tr. 214:16-25. These businesses and people are part of the public interest that must be considered just as much as the potential additional

employees by SMNG. There is no evidence that the benefits of natural gas will outweigh the losses to the propane and electric industry.

Allowing SMNG's expansion will negatively affect those propane users who do not convert to natural gas (and with the conversion cost tariff sheets, even for some who would like to, it may be cost-prohibitive). Residents and businesses that continue to use propane gas may very well see their costs increase due to the lower demand for propane. Less demand could result in terminal closures, driving up the costs of delivering propane to a particular area. Tr. 210:12-211:15. Also, if there are capacity issues in an area, there is often a wintertime (peak time) demand for propane to supplement natural gas. Tr. 206:16-210:8. When natural gas users are buying propane at the same time regular propane users need it, it drives the cost up on the wholesale market. Tr. 210:3-9. SMNG currently has 15 million cubic feet per day of firm delivery capacity with Southern Star Central Gas Pipeline ("Southern Star"). Exhibit 20. It contracted for 5 million cubic feet per day of that amount in December 2006. Tr. 63:20-64:4. There is currently no additional capacity available on Southern Star. Tr. 118:3-6. SMNG represents that the 15 million cubic feet per day is adequate capacity to serve the proposed expansion. ***Highly Confidential*** Additionally, the conversion of 50% of residential propane users is expected to take five years (Tr. 71:13-20, 97:16-20), but SMNG's projections of volume needed to serve customers only goes out through the end of 2007. Exhibit 6HC, spreadsheets titled "Recapitalization, Customer Information", under "Volumes." If SMNG needs additional capacity just a few years out, it does not have it, and Southern Star does not have it to offer. This would create a peak demand capacity issue for SMNG and surely it would supplement with propane, driving up propane costs for everyone in the winter months. This is not in the public interest.

CONCLUSION

SMNG has the burden to prove that this Commission should grant a CCN. SMNG has failed to present competent and substantial evidence to meet that burden. Because Of SMNG's failure to meet each of the Commission's standards, the Commission does not have the option, much less the obligation to grant SMNG's application.

WHEREFORE, the Missouri Propane Gas Association respectfully requests the Public Service Commission deny the Applications in the three consolidated cases.

Respectfully Submitted,

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CERTIFICATE OF SERVICE

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