BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

The Staff of the Missouri Public Service Commission,	)	
Complainant,	)	
v.	)	**Case No. GC-2006-0491**
Missouri Pipeline Company, LLC, and Missouri Gas Company, LLC,	)	
Respondents.	)	

REVISED REPORT AND ORDER

Issue Date: October 11, 2007
Effective Date: October 21, 2007

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The Staff of the Missouri Public Service Commission, Complainant, v. Missouri Pipeline Company, LLC, and Missouri Gas Company, LLC, Respondents.	)))))))))))	**Case No. GC-2006-0491**

Table of Contents

Appearances

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REGULATORY LAW JUDGE: Morris L. Woodruff, Deputy Chief Regulatory Law Judge

REVISED REPORT AND ORDER

Syllabus: The Commission is issuing this Revised Report and Order in response to the applications for rehearing filed by the Municipal Gas Commission of Missouri and Union Electric Company d/b/a AmerenUE. The changes to the order relate to certain conclusions of law regarding the interpretation of the tariffs of Missouri Pipeline Company and Missouri Gas Company relating to Count III of Staff's complaint

FINDINGS OF FACT

The Missouri Public Service Commission, having considered all the competent and substantial evidence upon the whole record, makes the following findings of fact. The positions and arguments of all of the parties have been considered by the Commission in making this decision. Failure to specifically address a piece of evidence, position, or argument of any party does not indicate that the Commission has failed to consider relevant evidence, but indicates rather that the omitted material was not dispositive of this decision.

Procedural History

On June 21, 2006, the Staff of the Commission filed a complaint against Missouri Pipeline Company, LLC (MPC), and Missouri Gas Company, LLC (MGC). The complaint contains six counts alleging that MPC and MGC have violated several aspects of their tariffs. Staff developed this case as an offshoot from a broader over-earnings complaint Staff filed against MPC and MGC, as well as several affiliated companies, on March 31, 2006. That over-earnings complaint was pending before the Commission as Case No. GC-2006-0378, but, at the request of Staff, was dismissed without prejudice on June 25, 2007.

By a notice issued on June 22, 2006, pursuant to Commission Rule 4 CSR 240-2.070(7), the Commission served a copy of Staff's complaint on MPC and MGC. That order also provided notice of the filing of Staff's complaint to the other parties to GC-2006-0378, and established an intervention deadline of July 12, 2006. Subsequently, Union Electric Company, d/b/a AmerenUE, and the Municipal Gas Commission of Missouri were allowed to intervene. MPC and MGC timely responded to Staff's complaint by filing their answer on July 21, 2006.

The Commission established a procedural schedule requiring the parties to prefile written direct, rebuttal, and surrebuttal testimony. An evidentiary hearing convened on December 13, and continued on December 14 and 15, 2006. Initial post-hearing briefs were submitted on February 9, 2007, with reply briefs following on February 20. Additional oral arguments were held on July 10, 2007.

The Operations of MPC and MGC

MPC and MGC own and operate interconnected, intrastate natural gas pipeline systems located in east central Missouri. The natural gas flowing through MPC's pipeline is obtained from two interconnections with interstate pipelines. The first interconnection is with Panhandle Eastern Pipeline Company in Pike County, Missouri. The MPC pipeline then runs south and east into St. Charles County, Missouri, where it terminates with a connection to Missouri Interstate Gas. Missouri Interstate Gas, in turn, owns and operates a 5.6-mile pipeline that runs under the Mississippi River and interconnects with a major interstate natural gas pipeline, Mississippi River Transmission, in Illinois. A branch of MPC's pipeline extends southwesterly from St. Charles County, through Franklin County, to a southern terminus at Sullivan, Missouri.

At Sullivan, the MPC pipeline connects with the pipeline owned and operated by MGC. The MGC pipeline then extends another 66 miles, terminating at the United States Army facility, Fort Leonard Wood. Along the way, MGC's pipeline also provides gas to the towns of St. James, Cuba, Waynesville, St. Robert, Rolla, Salem, and Owensville.[1]

MPC and MGC are transporters of gas, not sellers of gas. That means they collect a fee for transporting the gas that various shippers purchase from gas suppliers and move through the pipelines. Shippers on the pipeline include other public utilities, notably Laclede Gas Company and AmerenUE, who move gas through the pipelines for delivery to

[1] Ries Rebuttal, Ex. 304, Pages 4-5.

the homes and businesses of their customers. Other shippers are municipal gas distribution systems and large industrial users who purchase their own gas supply.

The Operations of Omega Pipeline Company

The third pipeline company that is important to Staff's complaint is Omega Pipeline Company. Omega owns and operates the natural gas distribution system on Fort Leonard Wood, a federal enclave. In its role as a local distribution company, operating exclusively at Fort Leonard Wood, Omega is not subject to regulation by this Commission.[2] However, after July 1, 2003, Omega was also used as a gas marketing company, providing gas-marketing services[3] to several entities that obtained natural gas through MPC or MGC. Omega's role as a gas marketer is the role about which Staff is concerned in its complaint.

Ownership of MPC, MGC, Omega, and Affiliated Companies

MPC and MGC, as well as Missouri Interstate Gas, are owned by United Pipeline Systems, Inc., which was formerly known as Utilicorp Pipeline Systems, Inc. United Pipeline is owned by Gateway Pipeline Company, LLC, which purchased the stock of Utilicorp Pipeline Systems in 2002, from the company now known as Aquila, Inc.[4] Moving up the corporate ownership chain, Gateway is ultimately owned by two individuals, Dennis Langley (85%) and David Ries (15%).[5] As sister corporations sharing a common ownership, MPC and MGC are "affiliated entities", as that term is defined by the

[2] The Federal government has exclusive jurisdiction over federal enclaves pursuant to Article I, Section 8 of the United States Constitution.

[3] Gas marketing services include purchase of gas supplies, administration of contracts, and monitoring of the nomination process required to transport gas,

[4] Id.

[5] Schallenberg Direct, Ex. 19, Schedule 3, Page 4.

Commission's affiliate transaction rule.[6] Along with MPC and MGC, Gateway also purchased Omega Pipeline Company from Aquila in 2002. Thus, until it was sold to Tortoise Capital Resources Corporation on June 1, 2006, Omega was also an affiliate of MPC and MGC.

Staff's Motion for Sanctions for Destruction of Documents

On November 14, 2006, Staff filed a motion asking the Commission to impose monetary sanctions against MPC, MGC, and their President, David Ries, for allegedly destroying certain invoices that Staff needs to support its case. In addition, Staff asked the Commission to apply the spoliation of evidence rule to make certain evidentiary inferences adverse to MPC and MGC. On December 5, after several rounds of written responses were submitted by MPC and MGC, as well as by Staff, the Commission informed the parties that it would take up Staff's motion as a part of the evidentiary hearing. The Commission also informed the parties that they would be allowed to present additional live direct testimony on that question. Much of the first day of the hearing was spent hearing testimony on Staff's motion.

In January 2006, early in its investigation, Staff sought production of invoices showing the bills that MPC and MGC sent to their customers.[7] At that time, David Ries informed Staff that those actual invoices were not retained in the companies' records.[8] Ries indicated that the original paper invoices were mailed to the customers and the companies did not retain a copy for their own records.[9] Instead, of invoices, Ries provided

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[6] Commission Rule 4 CSR 240-40.015(1)(A).

[7] A copy of Staff's subpoena to B. J. Lodholz, CFO/Comptroller for MPC and MGC is Ex. 251.

[8] Transcript, Pages 50-51, Lines 21-25, 1-12.

[9] Transcript, Page 146, Lines 8-16.

Staff with a revenue summary document for 2005.[10] That summary spreadsheet does not reveal the existence of additional customers being served through pipeline capacity held by the City of Cuba.[11] Subsequently, in June 2006, Staff obtained what it described as recreated invoices for 2004 and 2005 from MPC and MGC. Staff has never obtained 2003 invoices from MPC and MGC.[12] Ries testified in his deposition that the companies did not provide the 2003 invoices to Staff because "[w]e don't have any paper copies of them and it would require an extreme amount of effort and diligence to go back and recreate them."[13]

Since it could not obtain actual invoices from MPC and MGC, Staff contacted various customers, attempting to obtain copies of the invoices the customers received from MPC and MGC. Actual invoices received from Cuba revealed that some of the gas that MPC and MGC showed as delivered to Cuba was actually being delivered to other customers.[14]

Because of these inconsistencies, Staff suspected the accuracy of the recreated invoices, but continued to rely on the recreated invoices in developing its complaint. Then, on July 17, 2006, Staff deposed B. J. Lodholz, the former CFO/Controller of MPC and MGC. Lodholz revealed that he kept paper copies of the "summary sheet, the front page" of the invoices in his office. Lodholz indicated that he had kept those summary sheets all the way back to when he started working for MPC and MGC in July 2002.[15]

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[10] That spreadsheet is Ex. 53HC.

[11] Transcript, Pages 70-71, Lines 19-25, 1-8.

[12] Transcript, Page 91, Lines 20-22.

[13] This portion of Ries' deposition is Ex. 257, Page 700, Lines 23-25. The deposition was also read into the record at the hearing and may be found at Transcript, Page 106, Lines 1-3.

[14] Transcript, Page 57, Lines 12-23.

[15] This portion of Lodholz' deposition is Ex. 256, Page 191, Lines 3-20. It was read into the record at the hearing and may be found at Transcript, Pages 95-96, Lines 10-25, 1.

Believing they had now found the original invoices they were seeking, Staff directed Ries to bring those documents from Lodholz's files to his October 17, 2006, deposition. At his deposition, Ries produced actual copies of the face sheets from the invoices,[16] but indicated that the complete documents that Staff sought were not in Lodholz's files. Ries also suggested that perhaps the person who replaced Lodholz as controller had discarded the documents when he took over Lodholz's office.[17] Lodholz had left the employ of MPC and MGC on May 12, 2006.[18]

In its motion for sanctions, Staff accused Ries, or someone acting at his direction, of having deliberately destroyed the original invoices from 2003, 2004, and 2005. In response to Staff's motion for sanctions, MPC and MGC filed affidavits from Ries, Michael Mertz (Controller), David Wallen (V.P. Operations), and Patty Hawkins (Office Manager). All the affidavits indicated that the documents described by Lodholz in his deposition were only billing summaries, not the complete invoices sought by Staff. Each affiant also denied having destroyed any of Lodholz's documents after Lodholz left the company on May 12, 2006.[19]

At the hearing, MPC and MGC introduced an affidavit from Lodholz, which was admitted into evidence over the objection of Staff.[20] In his affidavit, Lodholz explained that

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[16] Transcript, Page 104, Lines 23-24.

[17] Transcript, Page 107, Lines 3-14.

[18] Transcript, Page 109, Lines 2-3.

[19] The four affidavits are Ex. 258.

[20] The Lodholz affidavit is Ex. 311. One of Staff's objections to the admission of the Lodholz affidavit was that the affidavit did not include a date indicating when it was executed. Approximately a month after the hearing, on January 16, 2007, MPC and MGC filed a re-executed affidavit from Lodholz that indicates it was signed on January 12, 2007. MPC and MGC filed an accompanying motion asking the Commission to substitute the re-executed affidavit for the originally admitted Exhibit 311. Staff opposed that motion. There is no basis for supplementing or substituting a new affidavit for the document previously admitted as Exhibit 311. MPC and MGC's motion will be denied.

the documents he referred to in his deposition were not the front page of the actual invoices. Instead, he had retained "a one page summary sheet for each month showing a list of the pipeline customers, the volume of gas delivered, the dollar charge by each of MPC and MGC, as well as the total aggregate charge to each customer for that month."[21] The summary sheets described by Lodholz are included with the affidavit as Exhibit 311. No party called Lodholz to testify at the hearing.

Based on the evidence presented, Staff failed to prove its allegations that documents retained by Lodholz were destroyed to avoid disclosing them to Staff. It appears that the documents described by Lodholz in his deposition, as clarified in his affidavit, were turned over to Staff. No monetary sanction for destruction of documents is appropriate. However, the adverse evidentiary inference sought by Staff requires scrutiny.

The Commission is troubled by MPC and MGC's failure to provide Staff with even recreated invoices for 2003. Section 393.140(4), RSMo 2000, and Commission Rule 4 CSR 240-10.010 require public utilities to maintain their vital records and to make those records available to the Commission for review. However, MPC and MGC claim that to provide Staff with copies of invoices sent to customers in 2003 would be unduly burdensome. This is not a question of retaining documents in electronic form rather than paper. It is certainly reasonable to dispose of paper and instead keep important documents in an electronic database. That is how the Commission retains its own files. However, it is unbelievable that MPC and MGC would produce invoices, mail those invoices to customers, and then fail to retain either a paper or electronic copy of such invoices in a readily accessible form.

[21] Ex. 311.

Staff did not prove that MPC and MGC deliberately destroyed those invoices, although that possibility is consistent with the circumstances. Staff certainly established that MPC and MGC's inability to produce original or electronic copies of customer invoices was very unusual.[22] Furthermore, Staff established that it had great difficulty obtaining needed documentation from MPC and MGC throughout its investigation.[23]

While Staff did not prove that the invoices were deliberately destroyed, the circumstances do establish that MPC and MGC were at least grossly incompetent in their retention of important records. Because of MPC and MGC's failure to maintain proper records for 2003, Staff was denied the evidence it needs to firmly establish the transportation rates charged to shippers on MPC and MGC's pipelines in 2003. The Commission will allow Staff to infer those rates, consistent with other evidence presented, as explained later in this Report and Order.

Regulation by the FERC

On June 28, 2006, Missouri Interstate Gas, along with MPC and MGC filed an application with the Federal Energy Regulatory Commission for authority to reorganize themselves to be reconstituted as an interstate pipeline, subject to the exclusive jurisdiction of the FERC. On April 20, 2007, the FERC issued an order granting that application and issuing federal certificates to the reorganized interstate pipeline.[24] Staff and other parties have sought rehearing of the FERC's decision, but, if the FERC's order stands, MPC and MGC will no longer be subject to regulation by this Commission.

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[22] Transcript, Page 62, Lines 15-18.

[23] Transcript, Pages 125-126, Lines 20-25, 1-5.

[24] FERC Docket No. CP06-407-000, et. al.

However, this case is not moot because Staff's complaint alleges MPC and MGC violated their tariffs at a time when those companies were undeniably subject to regulation by this Commission. Therefore, the Commission will render a decision on Staff's complaint.

The Allegations of Staff's Complaint

Count 1

Findings of Fact

The first count of Staff's Complaint alleges that MPC and MGC failed to maintain separate facilities and personnel from Omega, as a marketing entity, thereby violating their own tariffs. In doing so MPC and MGC also failed to abide by the Commission's regulation regarding affiliate transactions.

David Ries is president of MPC and MGC. In addition, he was president of Omega until it was sold on June 1, 2006.[25] Staff alleges Ries used his position as the head of these companies to negotiate arrangements between the companies in a way that favored Omega over other companies that were shipping gas on the MPC and MGC pipelines. Staff alleges that, acting through Ries, MPC and MGC failed to apply their tariff terms, conditions, and requirements in a uniform and non-discriminatory manner to non-affiliated shippers. In particular, Staff alleges that MPC and MGC improperly shared confidential information with Omega, failed to require Omega to balance its gas shipments on the pipelines, while requiring all other shippers to do so, and allowed Omega to take possession of and sell lost and unaccounted for gas that accumulated on the pipeline.

The tariffs of MPC and MGC provide that MPC and MGC share office space with its affiliates, which would include Omega. However, those tariffs also indicate that MPC and

[25] Transcript, Page 509, Lines 3-14.

MGC, as transporters of gas, maintain "separate operational facilities and personnel" from their affiliates. The tariffs also promise that "operational and accounting information is confidentially maintained by Transporter."[26]

The evidence demonstrates that, as president of MPC, MGC, and Omega, Ries was given daily access to information that could benefit Omega in its role as a marketing agent. Staff submitted a sample of the daily reports Ries received as Exhibit 21. As described by Staff's witness, Robert Schallenberg, that daily report contains:

> information regarding the shippers, all the shippers on the pipeline. It identifies their agent or when they're acting as their own agent. It identifies their contract number to the extent this is one for its shipments. And then it tells you what its current status is regarding the gas that's brought into the system on the day and the in balance [imbalance]. And then it shows cumulative information.[27]

That same information was not shared with other shippers on the pipelines, including other entities that were acting as marketing agents in competition with Omega.[28] Having access to that sort of information provided Omega with a competitive advantage over the other marketing agents who shipped gas on MPC and MGC allowing Omega access to market information and price information of competitors, other shippers could not access. [29] In a game of cards it would be like one player being able to see the cards of others at the table.

MPC and MGC do not deny that as president of Omega, Mr. Ries had access to the same information about the operations of the pipelines that he could access as president of MPC and MGC. Instead, in their defense, MPC and MGC argue that the Commission's Staff has long been aware of the affiliate relationship and shared employees and officers

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[26] Ex. 70, MGC's tariff, P.S.C. Mo. No. 2, Sheet No. 39; and Ex. 71, MPC's tariff, P.S.C. Mo. No. 3, Sheet 39.

[27] Transcript, Page 293, Lines 13-20.

[28] Transcript, Page 265, lines 1-3.

between Omega and MPC and MGC, and did not raise any objection to that relationship until it filed this complaint.

MPC and MGC explain that they wanted to provide a bundled service to some small customers of the pipelines and were looking for a way to do that consistent with their tariffs.[30] However, those tariffs do not allow them to buy or sell gas; they are only allowed to operate as transporters of gas. On August 23, 2002, Ries contacted Staff by e-mail and indicated MPC and MGC were considering either the revision of its tariffs to allow for the sale of gas to customers, or as an alternative, the use of Omega to provide a marketing service to customers along the path of the pipelines.[31] Staff responded to Ries' proposals in a letter dated January 3, 2003.[32]

MPC and MGC contend that Staff's letter indicates Staff knew of and approved the plan to use Omega as a marketing affiliate.[33] In particular, MPC and MGC point to one sentence of that letter that states, "In previous conversations, Staff has expressed concern over the structure of these transactions and Staff's preference that an affiliate should make any 'bundling' arrangements."[34] From that sentence, MPC and MGC contend Staff knew of and approved their plan to use Omega to market gas.

That interpretation is not, however, supported by the rest of the Staff's letter. The next sentence of the letter states:

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[29] Transcript, Page 278, Lines 10-20.

[30] Transcript, Page 574, Lines 2-19.

[31] Ex. 310.

[32] Ex. 308.

[33] Transcript, Page 593, Lines 14-22.

[34] Ex. 308.

> Even if an affiliate engages in these transactions, however, Staff has concerns that separation between regulated and unregulated operations will not exist due to the structure of MPC, MGC, MIG, and Omega.

Clearly, in 2003, Staff had concerns about the improper sharing of information between MPC and MGC and a marketing affiliate. It is precisely those concerns that Staff brought to the Commission's attention in this complaint. Thus, the January 3, 2003, letter cannot reasonably be interpreted as indicating Staff's approval of the use of Omega as a marketing affiliate of MPC and MGC.

Even if Staff had fully approved MPC and MGC's use of Omega as a marketing affiliate, that approval would not absolve MPC and MGC of their duty to comply with the requirements of their tariffs. Those tariffs require MPC and MGC, while acting as transporters of gas, to maintain the confidentiality of operational and accounting information. Instead, they shared that information with Omega through the shared presidency of David Ries.

As further support for Count I, Staff contends that MPC and MGC gave special preference to Omega when they did not require Omega to balance its daily use of pipeline capacity. Omega, in its role as a local distribution company supplying gas to Fort Leonard Wood, as well as in its role as a gas marketer for other customers, shipped gas on the pipeline system. The tariffs of MPC and MGC require a shipper on the system to balance the amount of gas it puts into the pipeline with the amount of gas it takes out each day, within a ten percent tolerance range.[35] AmerenUE, another shipper on the pipelines, was required to comply with this requirement.[36] MPC and MGC did not require Omega to balance its nomination and usage of gas supplies. On many days, Omega did not

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[35] Exhibits 70 and 71.

nominate any gas into the pipeline, while continuing to deliver gas to its customers at the other end of the pipeline.[37] As would be expected, Omega accumulated a substantial imbalance while it was affiliated with MPC and MGC.[38]

MPC and MGC agree that Omega was not required to balance its gas nominations and usage. However, they contend that by undertaking to balance the overall gas flows on the pipeline system, Omega was performing a valuable service that benefited the pipeline companies and ultimately their other customers.

MPC and MGC explain that pipeline imbalances result from the difference between the volume of gas that a shipper or its agent nominates from the interstate delivering pipeline, and the volume of gas actually used by the shipper. For MPC and MGC, the delivering pipelines are Panhandle Eastern Pipeline Company (PEPL) and Mississippi River Transmission (MRT). A shipper contracts with PEPL or MRT to deliver a certain amount of gas into the MPC and MGC pipeline system. The shipper then uses a certain amount of gas from the MPC and MGC pipeline system at the other end. To the extent the amount of gas used by the shipper differs from the amount put into the pipeline from the interstate pipeline, the MPC and MGC pipeline system is out of balance.

MPC and MGC are gas transporters, not gas merchants, and their tariffs do not allow them to buy or sell gas for any reason.[39] As a result, MPC and MGC cannot buy or sell gas off their pipelines to balance the system if the shippers bring too much, or too little, gas into the system. MPC and MGC argue that they used their affiliate, Omega, to balance

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[36] Transcript, Page 266, Lines 1-22.

[37] Ex. 21HC is a sample imbalance summary for a particular date showing the imbalance sustained by Omega and its customers, compared to non-affiliated shippers on the pipeline system.

[38] Transcript, Page 548, Lines 1-14. The exact numbers are highly confidential.

the system. The pipelines suggest that Omega would reduce its nominations when there was otherwise too much gas in the system, and increase its nominations if other shippers nominated too little gas.[40]

However, there were generally excess amounts of gas in the pipeline system. The real objective of this scheme, as will be explained, was that Omega was able to extract unregulated profits by selling that accumulated gas to its customers. Through the use of inside information, Omega appears to have also acquired access to additional gas at no cost.

The transportation contracts that MPC and MGC enter into with the various shippers allow the pipelines to retain a certain percentage of the nominated gas as gas lost or unaccounted for during the transportation process.[41] For example, MPC and MGC's contract with AmerenUE, which is a shipper on the pipelines, required AmerenUE to nominate at various times an extra .43 to .50 percent when shipping gas through the pipeline to compensate for lost and unaccounted for gas.[42] The amount of gas nominated to compensate for lost and unaccounted for gas can vary from contract to contract depending upon the needs of the system and the negotiating position of the parties.[43]

Some gas is inevitably lost while it is being transported through the pipeline, but to the extent the gas lost is less than the extra nomination required by the contract, lost and unaccounted for gas can accumulate on the system. There was testimony that the extra

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[39] Ries Rebuttal, Ex. 304, Page 9, Lines 18-19.

[40] Ries Rebuttal, Ex. 304, Page 12, Lines 10-13.

[41] Transcript, Page 531, Lines 17-22.

[42] Transcript, Page 269, Lines 15-17.

[43] Transcript, Page 270, Lines 6-11.

gas on the system belongs to the pipeline company [44]. However the contracts governing lost and unaccounted for gas were not introduced into evidence While title to the gas was not clearly established in this case, MPC and MGC's tariffs do not allow them to sell gas for any reason. To get around that problem, MPC and MGC allowed its marketing affiliate, Omega, to under-nominate the amount of gas it put into the pipeline. Omega was then able to deliver more gas to its marketing customers than it put into the system, while collecting payment from the customers for all the gas it delivered. In effect, Omega was thereby able to sell that lost and unaccounted for gas to its marketing customers, with the proceeds ultimately flowing back to the owners of MPC, MGC, and Omega.

This arrangement clearly provides an advantage to Omega as it competes with other marketers to provide service to customers along the length of the pipeline. It may have also resulted in harm to other entities doing business with the pipeline if MPC and MGC had an obligation to notify those entities that the estimated percent of lost and unaccounted for gas was higher than that experienced or to adjust the estimate downward.

The advantage MPC and MGC gave to their affiliate is increased by the inappropriate sharing of confidential information, and explains the likely reason that information was shared. Since David Ries, as President of Omega, had full access to the confidential records of MPC and MGC, he knew exactly how much gas other shippers were nominating for shipment through the pipeline. With that knowledge, he also knew how much extra lost and unaccounted for gas would be available for Omega to sell to its customers.

[44] Transcript, Page 270, Lines 20-25.

Because Omega was not required to balance its gas nominations and usage, it accumulated an imbalance of more than $1 million worth of gas.[45] So long as Omega was owned by the same people that owned MPC and MGC, that imbalance represented additional unregulated profit that could be hidden from regulators charged with examining MPC and MGC's income to set the rates they could charge their customers. It also provided significant advantage to Omega in competing with other entities.

Conclusions of Law

1. Section 12.b of the General Terms and Conditions of the tariffs issued by MPC and MGC provides:

> For efficiency purposes, Transporter occupies office space on the same floor as its affiliates, but maintains separate operational facilities and personnel. Operational and accounting information is confidentially maintained by Transporter.[46]

2. Section 2.b of the General Terms and Conditions of the tariffs issued by MPC and MGC provides in relevant part: "If, due to operating conditions, the quantities of gas received and delivered are not in balance on any one particular day, such imbalance shall be corrected as promptly as is consistent with operating conditions."[47] This section of the tariff requires all shippers on the pipeline to balance the gas they put into the pipeline with the gas they take out on a daily basis.

3. The Commission's Affiliate Transaction rule for gas utilities, 4 CSR 240-40.015(1)(A), defines an affiliated entity as "any person, including a … corporation … which directly or indirectly, through one (1) or more intermediaries, controls, is controlled by, or is

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[45] Transcript, Page 548, Lines 10-14.

[46] Exhibits 70 and 71, Tariff Sheet No. 39.

under common control with the regulated gas corporation." Until it was sold on June 1, 2006, Omega met the definition of an entity affiliated with MPC and MGC.

4. Commission Rule 4 CSR 240—40.015(2) provides:

> (A) A regulated gas corporation shall not provide a financial advantage to an affiliated entity. For purposes of this rule, a regulated gas corporation shall be deemed to provide a financial advantage to an affiliated entity if-
> 1. It compensates an affiliated entity for goods or services above the lesser of-
> A. The fair market price; or
> B. The fully distributed cost to the regulated gas corporation to provide the goods or services for itself; or
> 2. It transfers information, assets, goods or services of any kind to an affiliated entity below the greater of-
> A. The fair market price; or
> B. The fully distributed cost to the regulated gas corporation.
> (B) Except as necessary to provide corporate support functions, the regulated gas corporation shall conduct its business in such a way as not to provide any preferential service, information or treatment to an affiliated entity over another party at any time.

5. MPC and MGC violated Commission Rule 4 CSR 240-40.15(2)(B)'s prohibition on affiliate transactions in that:

A) MPC and MGC provided preferential service information and or treatment:

1) By sharing confidential pipeline operations information with Omega;

2) By not requiring Omega to operate in balance within the parameters of its tariffs while requiring all other entities to do so; and

3) By allowing Omega to sell lost and unaccounted for gas.

B) MPC and MGC, violated provisions of Commission Rule 4 CSR 240-40.15(2)(A) by transferring gas to Omega at a price lower than the greater of fair market price or cost.

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[47] Exhibits 70 and 71, Tariff Sheet No. 26.

Decision

Did MPC and MGC violate the terms of their tariffs and Commission affiliate transactions rules (4 CSR 240-40.016) by permitting Omega Pipeline Company to use confidential customer information in a discriminatory manner for each of Omega's contracts with customers served by MPC and MGC and by allowing gas to be transferred to Omega at an amount lower than the greater of full market value or cost.

The evidence shows that MPC and MGC operated in a manner that gave their marketing affiliate, Omega, complete access to what should have been confidential information about the natural gas nominations made by and actual gas used by other shippers on the pipeline. Access to that information allowed Omega to adjust its own gas nominations to avoid the need to nominate any gas on many days. This allowed Omega to profit from the sale of lost and unaccounted for gas . With such inside information and preferential treatment, Omega had an unfair advantage in competing for customers. The improper sharing of confidential information violated the terms of MPC and MGC's tariffs. The improper transfer of utility assets to an affiliate without consideration violated the Commission's affiliate transactions rule. Allowing Omega to operate in violation of its tariff requirements for imbalance provided Omega with preferential treatment

MPC and MGC did not maintain separate operational facilities or personnel from Omega, in its role as an affiliated marketing entity. Beginning in 2003, David Ries was part-owner and president of MPC and MGC, as well as Omega. Ries negotiated gas sales and transportation arrangements with municipalities and other end-users for Omega, and then determined the MPC and MGC transportation arrangements that would apply to the Omega gas transactions. In his role with MPC and MGC, Ries gained inside knowledge of pipeline information such as pipeline gas imbalances, lost and unaccounted for gas levels, actual daily gas demand, and information about other shippers that is not available to any other shipper on the MPC and MGC pipeline system. Ries used this information to enter into transportation arrangements that were advantageous to Omega. Those advantageous arrangements were not made available to other shippers. Staff proved Count I of its complaint.

<u>Count II</u>

Findings of Fact

The second count of Staff's complaint alleges that MPC and MGC violated their tariffs by transporting gas to certain customers without obtaining a signed transportation agreement with those customers. The customers in question are G-P Gypsum Corporation and Willard Asphalt Paving, Inc., two large industrial users of natural gas, located along the pipeline route.

As explained more fully in the Conclusions of Law section of the Report and Order, MPC and MGC's tariffs state that the companies will provide gas transportation service to shippers who have executed a transportation agreement.[48] MPC and MGC transported gas to meet the needs of the two industrial customers, but never entered into a Transportation Agreement with either of them. MPC and MGC acknowledge transporting gas to serve these customers, but contend that no transportation agreement was necessary because the gas supplied to those customers was transported under the terms of a transportation agreement with the City of Cuba.

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[48] Imhoff Direct, Ex. 1, Page 5, Lines 2-4.

The City of Cuba has had valid Transportation Agreements with MPC[49] and MGC[50] since at least July 1, 1999, a date before MPC and MGC were purchased by their current owners. Beginning on July 1, 2003, Omega entered into a marketing agreement with Cuba.[51] Subsequently, Omega entered into separate marketing agreements with the two industrial customers.[52] These marketing agreements are the basis for MPC and MGC's argument that it can transport gas to G-P Gypsum and Willard Asphalt without a separate transportation agreement.

Gas marketing agreements are common in the natural gas industry. Under such an agreement, a relatively small municipal gas system or industrial customer hires an experienced gas marketer to purchase their gas supply, administer contracts, and monitor the nomination process to transport the gas to their customers.[53] The field of gas marketing is competitive and is not regulated by this Commission. Indeed, other gas marketers currently provide service to other small towns along the MPC and MGC pipelines,[54] and such towns do not have separate transportation agreements with the pipeline.[55]

In general, there is nothing wrong with gas marketing agreements. Such agreements only become problematic when the gas marketer is in an affiliate relationship with a pipeline company. The problem is, such a gas marketing agreement by an affiliate

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[49] Cuba's Transportation Agreement with MPC is Ex. 23HC.

[50] Cuba's Transportation Agreement with MGC is Ex. 24HC.

[51] Omega's marketing contract with Cuba is Appendix I to Ries Rebuttal, Ex. 304.

[52] Omega's marketing contract with G-P Gypsum took effect on August 1, 2003, and is Ex. 32. Omega's marketing contract with Willard Asphalt took effect on April 1, 2004 and is Ex. 33.

[53] Smith Rebuttal, Ex. 303, Page 10, Lines 14-22.

[54] Smith Rebuttal, Ex. 303, Page 11, Lines 16-21.

of a pipeline utility allows the utility to hide transportation discounts given to an unregulated marketing affiliate. A pipeline utility negotiating a transportation agreement with a gas marketing affiliate has a strong incentive to slash its transportation rates for an affiliate, since the money ultimately ends up in the same pocket.

The unregulated gas marketing affiliate that receives the benefit of reduced transportation rates can offer a portion of those saving to prospective customers, thereby gaining a competitive advantage over other gas marketers seeking to serve the same customers. Meanwhile, the utility's regulated rates will be based, in part, on the income earned by the utility. To the extent that the regulated utility's income from providing transportation is transferred to an unregulated affiliate, the regulated rates of the utility will need to be increased. Ultimately, the customers served by the utility could be required to pay the cost of the transportation discounts given to the marketing affiliate.

MPC and MGC's tariff states that transportation services are to be provided to any shipper who enters into a transportation agreement. The tariffs do not define "shipper," and MPC and MGC would circularly define a "shipper" simply as someone who has entered into a transportation agreement. By their definition, a gas customer who receives deliveries of gas under some other customer's transportation agreement is not a "shipper" and does not need to enter into a transportation agreement. That definition makes sense in the context of an unaffiliated gas marketer, but it does nothing to prevent the previously described affiliate abuse problem.

Staff would apply a definition of "shipper" taken from the Commission's marketing affiliate transaction rule, 4 CSR 240-40.016(1)(M). That section defines "shipper" to include

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[55] Ries Rebuttal, Ex. 304, Page 18, Lines 14-23.

"all current and potential transportation customers on a regulated gas corporation's natural gas distribution system." If that definition were applied to MPC and MGC's tariffs, then Staff would read the tariff as limiting the provision of transportation service to those end-use customers who have entered into a transportation agreement. The consistent application of Staff's definition to the tariffs would also, effectively bar all gas marketers, unaffiliated as well as affiliated, from the MPC and MGC pipelines unless the marketer's customers enter into a separate transportation agreement with the pipelines.

Conclusions of Law

1. MPC and MGC's tariffs contain two provisions that define when transportation service is to be available to any shipper. For Firm Provisional Transportation Service, the clause is found in Section 1, Tariff Sheet No. 4. For Interruptible Provisional Transportation Service, the clause is found in Section 1, Tariff Sheet No. 15. Both tariff sheets state in relevant part as follows:

> 1. . . . Such transportation service shall be available for any Shipper:
>
> . . .
>
> c. which has executed a Transportation Agreement wherein Transporter has agreed to transport natural gas for Shipper's account up to a specific maximum daily transportation volume. . . .

2. The definition section of the Commission's Marketing Affiliate Transactions Rule states: "Shippers means all current and potential transportation customers on a regulated gas corporation's natural gas distribution system."[56] Although it could have done so, the Commission did not include a provision in the Marketing Affiliate Transactions Rule requiring all shippers - defined as all current and potential transportation customers - on a

[56] Commission Rule 4 CSR 240-40.016(1)(M).

pipeline to execute a separate transportation agreement before receiving natural gas delivered through the pipeline.

Decision

Did MPC and MGC violate their tariffs by transporting natural gas to certain Omega customers without an executed transportation agreement?

Staff would interpret MPC and MGC's tariff as requiring every current or potential transportation customer who receives natural gas delivered through the pipeline to have executed a transportation agreement. Staff would then seek penalties against MPC and MGC for having violated this interpretation of their tariff.

Staff's interpretation of the tariff is not consistent with industry practice in that customers of non-affiliated gas marketers generally do not need to have a separate shipping agreement with the pipeline. Indeed, Staff does not attempt to apply such an interpretation to natural gas deliveries to customers through gas marketers not affiliated with MPC and MGC. Staff bases its interpretation on a definition of shipper taken from the context of the Commission's Marketing Affiliate Transactions Rule, but does not offer a consistent basis for applying that definition outside the confines of that narrow rule.

Staff describes a legitimate concern about abuse of the affiliate relationship engendered by the concealment of transportation discounts given to a gas marketing affiliate. The Commission will address that concern again in a broader context in Count III of Staff's complaint. However, within the narrower parameters of Count II of Staff's complaint, the Commission must find that the language of MPC and MGC's tariff's do not require every current or potential transportation customer who receives natural gas delivered through the pipeline to have executed a transportation agreement. MPC and

MGC did not violate that provision of their tariffs by transporting gas to such customers, and relief on Count II of Staff's complaint will be denied.

Count III

Findings of Fact

The third count of Staff's complaint alleges MPC and MGC offered certain transportation discounts to Omega, at a time when Omega was an affiliated company. MPC and MGC's tariffs provide that "the lowest transportation rate charged to an affiliate shall be the maximum rate that can be charged to non-affiliates."[57] Staff claims the discounts MPC and MGC gave to Omega set a new lower standard for the amount MPC and MGC could charge non-affiliated companies for transportation service. Staff asks the Commission to adjust MPC and MGC's rates accordingly.

When evaluating Staff's claim, the Commission must determine whether MPC and MGC gave a discount to Omega. While it was affiliated with MPC and MPC, Omega operated in two roles. Initially, beginning in 1992, long before the companies were purchased by their current owners, Omega owned the natural gas distribution system on the federal enclave of Fort Leonard Wood, and sold gas to the Fort under a marketing contract. In that role, Omega entered into a transportation agreement with MPC and MGC to transport natural gas to Fort Leonard Wood.[58] At that time, MPC, MGC, and Omega were owned by Utilicorp, n/k/a Aquila. Omega's marketing contract with Fort Leonard Wood expired on September 30, 2002, and Omega did not sell gas to the Fort from October 1, 2002, through January 31, 2005. Omega regained the contract with the Fort on

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[57] Tariff Sheet No. 6, Section 3.2b(1), Exhibits 70 and 71.

February 1, 2005, and once again transports gas through the pipelines for sale to the Fort.[59]

Omega's other role began on July 1, 2003, when its Natural Gas Sales and Agency Agreement with the City of Cuba went into effect.[60] Under that agreement, Cuba agreed to pay Omega "a fixed fee of **. . .** per Dth of Gas delivered to reimburse Seller [Omega] for all transportation fees (reservation and commodity) incurred by Seller on all upstream pipelines to transport said Gas purchased hereunder to the Delivery Point [the Cuba City Gate]."[61] That contract also appointed Omega as Cuba's agent to "nominate and administer the transportation of natural gas and pay the monthly invoices for the transportation services provided by MPC and MGC, and any other third party transporter, exclusive of the fuel charge." The contract required Cuba to reimburse Omega for the actual cost of the gas purchased under the contract. The gas that Omega purchased on behalf of Cuba was moved through the pipelines using the capacity reserved by Cuba under the 1999 Transportation Agreements between Cuba and MPC[62] and MGC.[63] By entering into this sales and agency agreement with Cuba, Omega became an affiliated gas marketer.

Before July 1, 2003, MPC and MGC charged the maximum tariff rates for transportation service for all shippers as shown in the following chart:[64]

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58 Ries Rebuttal, Ex. 304, Page 6, Lines 5-11.

59 Id. at Page 6, Lines 12-17.

60 Ex. 22.

61 Id. The amount of the fixed fee is highly confidential.

62 Ex. 23.

63 Ex. 24.

64 The chart is taken from Schallenberg Direct, Ex. 19, Page 24, Lines 4-11.

Transportation Type/ Delivery Points	Firm	Firm	Interruptible
	Reservation per MDQ	Commodity Per Dt.	Commodity Per Dt.
MPC Delivery	$4.3181	$.1699	$.3036
MGC Delivery Except the Fort	$13.1766	$.9433	$1.3765
MGC Delivery to the Fort	$18.10	$.55	$1.15

After July 1, 2003, MGC began charging Omega a reduced commodity charge of $.20 for delivering gas to Cuba. That rate is demonstrated by recreated invoices supplied by MGC. Specifically, Exhibit 67-E, which is comprised of recreated invoices for services beginning in January 2004, shows a commodity charge of $.20 for contract number MG-1009-TAF. That contract number is the Transportation Agreement with Cuba as shown in Exhibit 24.

The recreated invoices in evidence only go back to January 2004, MPC and MGC refused to produce such invoices for 2003.[65] For reasons previously explained in detail in its discussion of Staff's motion for sanctions for destruction of documents, the Commission will infer that if such invoices were available, they would show that Omega began receiving the discount on July 1, 2003.

In their defense, MPC and MGC contend they gave the transportation discount to the City of Cuba and not to Omega. Obviously, the City of Cuba is not affiliated with MPC and MGC, so a discount given to Cuba would not need to be extended to non-affiliated shippers.

In support of their contention that the discount was given to the City of Cuba, MPC and MGC point to a letter from David Ries, as President of MPC, to the Mayor of Cuba,

[65] Transcript, Page 92, Lines 20-22.

dated July 7, 2003.[66] The letter purports to memorialize a previous discussion in which MPC agrees to give Cuba a discounted commodity rate. However, unlike other letters from Ries purporting to memorialize discussions with municipalities about discounts, the July 7, 2003, letter to Cuba does not contain a signature from the recipient accepting and agreeing to the modification. Unlike those letters, the July 7, 2003, letter is not even formatted to contain such a signature.[67] These inconsistencies lead to the conclusion that Exhibit 26 was created after the fact to bolster MPC and MGC's position.

MPC and MGC also contend Omega was merely acting as an agent for Cuba in purchasing natural gas for the city and then transporting that gas to Cuba using the city's transportation agreement with the pipelines. However, that transportation agreement, which has been in effect since 1999, before MPC and MGC were purchased by their current owners, requires Cuba to pay full tariff rates to transport gas on the pipelines.[68] The sales and agency agreement between Cuba and Omega requires Cuba to pay a fixed fee to reimburse Omega for the cost of transporting gas through the pipelines.[69] The invoices, which show the amount Omega was actually billed for the transportation of gas to Cuba, allowed Staff to discover the discounted commodity charge that was given to Omega.. In sum, Omega was charging Cuba the transportation costs set in the sales and agency agreement, while paying MPC and MGC the discounted commodity charge identified by Staff. Omega kept the difference as extra profit.

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[66] Ex. 26.

[67] For comparison see Ex. 25, an August 9, 2002 letter to Cuba; Ex. 27, an April 12, 2006, letter to the City of Waynesville; and Ex. 28, a December 18, 2002 letter to Waynesville.

[68] Exhibits 23 and 24.

[69] Ries Rebuttal, Ex. 304, Appendix I.

Furthermore, MPC and MGC point out that the gas moved to the other Omega customers, G-P Gypsum and Willard Asphalt, was moved using the pipeline capacity of Cuba. They suggest that somehow that fact means that the transportation discounts they offered were made to a non-affiliated shipper. However, Omega's marketing contract with Cuba did not give it any authority to use Cuba's pipeline capacity to deliver gas to other customers. MPC and MGC's tariffs did not contain any provisions that would allow Cuba to release its capacity for the use of other shippers.[70] Ries, testifying on behalf of MPC and MGC conceded that Cuba likely did not even know that its capacity was being used in this manner.[71]

As MPC and MGC explain, there would be nothing wrong with this arrangement if Omega was not an affiliate of MPC and MGC. As an unregulated gas marketer, Omega is free to make a profit by marking up charges for elements of the bundled marketing services it provides to Cuba, and other shippers. Generally if a gas marketer can negotiate a better deal with the pipelines, it is welcome to keep the difference between what it pays the pipeline and what it collects from its customer as profit generated by its skills as a negotiator.

However, Omega was an affiliate of MPC and MGC. David Ries was President of both Omega and the pipeline companies. Therefore, he was on both sides of the negotiation and was in a position to grant himself a shipping discount. By giving the unregulated affiliate, Omega, a shipping discount, Ries could transfer income from the regulated utilities to the unregulated affiliate. Subsequently, in any future rate case, the regulated utilities would be in a position to justify charging higher rates to their captive

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[70] Transcript, Page 650, Lines 12-16.

customers. Furthermore, the increased profit made possible by the discounted transportation rates, would allow Omega to offer a better deal to the municipalities and other shippers to whom it was offering its marketing services, thereby gaining a competitive advantage. It is exactly this sort of affiliate abuse that MPC and MGC's tariff is seeking to prevent when it requires that shipping discounts given to an affiliate also be passed on to non-affiliates.

In their defense, MPC and MGC argue that Omega has consistently paid the highest rates of any shipper on the Pipelines' systems. In support of this claim, MPC and MGC offered the testimony of Christopher John, a former technical advisor at the FERC. John presented calculations, based on the 25 percent load factor specified in the tariff, which combined the reservation and commodity rates into a single volumetric transportation rate. His calculations show that from February 2005 through March 2006, Omega was charged a combined transportation rate of $2.6803/Dth, which was the highest transportation rate on the system.[72]

The principle flaw in John's argument is that his calculation reflects the transportation rate paid by Omega under the contract between MGC and Omega for transportation of gas to Fort Leonard Wood. It does not reflect the rates Omega paid to transport gas to customers other than Fort Leonard Wood. Since Fort Leonard Wood is located at the terminal end of the MGC pipeline, it is to be expected that Omega would be charged the highest rates of any shipper for transporting gas to the end of the pipeline. In contrast, the recreated invoices contained in Exhibit 67, Appendix E, show that when

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[71] Transcript, Page 651, Lines 12-16.

[72] John Rebuttal, Ex. 300, Page 26, Table beginning at Line 12.

transporting gas to the City of Cuba, Omega was charged a combined volumetric transportation rate of $1.9328/Dth, which was the lowest rate on the pipeline system.

As of July 1, 2003, the lowest rates MPC and MGC were charging Omega, an affiliated shipper, are shown in the following chart:[73]

Transportation Type/ Delivery Points	Firm	Firm	Interruptible
	Reservation per MDQ	Commodity Per Dt.	Commodity Per Dt.
MPC Delivery	$4.3181	$.1699	$.3036
MGC Delivery Except the Fort	$13.1766	**$.20**	$1.3765
MGC Delivery to the Fort	$18.10	$.55	$1.15

The previously discussed discount was just the first given by MPC and MGC to Omega. On September 1, 2003, MPC and MGC began providing discounted interruptible transportation service to Omega to allow Omega to provide bundled natural gas service to G-P Gypsum.[74] Subsequently, Omega entered into a similar agreement with Willard Asphalt Paving, Inc., effective April 1, 2004.[75] At that time, Omega did not have a separate Transportation Agreement with MPC and MGC relating to its role as a gas marketer. Instead, it moved gas through the pipelines to G-P Gypsum and Willard Asphalt using Cuba's Transportation Agreements.

Exhibits 35 and 36 are recreated invoices that illustrate the rates Omega, as a marketing affiliate, was charged to transport gas for G-P Gypsum and Willard Asphalt.

[73] The chart is taken from Schallenberg Direct, Ex. 19, Page 25, Line 1.

[74] Omega's Natural Gas Sales Agreement with G-P Gypsum is Ex. 32. The sales agreement states that it became effective on August 1, 2003, but it was not executed until August 19, 2003. Staff based its calculations on the assumption that the agreement became effective on September 1. The Commission will do the same.

[75] Omega's Natural Gas Sales Agreement with Willard Asphalt is Ex. 33.

Rather than send a separate bill to Omega for each of its marketing customers, the pipeline charges are included on a single bill, with detail that allowed Omega to determine the volumes delivered to each of its customers. Exhibits 35 and 36 show a total delivery of 11,077 Dths to three customers; 2,003 Dths were delivered to the Willard Asphalt interconnect, 5,565 Dths were delivered to the Cuba city gate on behalf of G-P Gypsum, and 3,509 Dths were delivered for use by the City of Cuba.

The invoice to Omega shows that the same commodity rates were charged for all volumes transported. Specifically, MPC and MGC charged Omega a MGC commodity rate of $.20/Dth, and a MPC commodity rate of $.1699/Dth. However, while the gas transported for Cuba was under firm transportation, the gas transported for G-P Gypsum was interruptible in nature,[76] as was that supplied to Willard Asphalt.[77] Thus, while the gas was delivered using the capacity reflected in the firm transportation contract between the pipelines and Cuba, the transportation service provided to G-P Gypsum and Willard Asphalt was actually interruptible. Since interruptible service does not provide for guaranteed capacity on the pipeline, there is no reservation charge. Therefore, the only charges reflected on the invoice for charges related to the transportation of gas to G-P Gypsum and Willard Asphalt is the MGC commodity rate of $.20/Dth and the MPC commodity rate of $.1699/Dth.

As of September 1, 2003, the lowest rates MPC and MGC were charging Omega, an affiliated shipper, are shown in the following chart:[78]

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[76] Schallenberg Surrebuttal, Ex. 67, Page 9, Lines 9-13.

[77] Ex. 33.

[78] The chart is taken from Schallenberg Direct, Ex. 19, Page 25, Line 15.

Transportation Type/ Delivery Points	Firm	Firm	Interruptible
	Reservation per MDQ	Commodity Per Dt.	Commodity Per Dt.
MPC Delivery	$4.3181	$.1699	**$.1699**
MGC Delivery Except the Fort	$13.1766	**$.20**	**$.20**
MGC Delivery to the Fort	$18.10	$.55	$1.15

On February 1, 2005, MGC began giving Omega an additional discount for the transportation of gas to Fort Leonard Wood. MGC's tariff establishes a maximum $.55/Dth commodity charge for firm transportation service to Fort Leonard Wood.[79] However, the invoices collected in Exhibit 67-D show that beginning on February 1, 2005, when Omega regained the contractual right to supply gas to the Fort, Omega was actually billed a commodity rate of $.30/Dth for firm transportation service to Fort Leonard Wood.[80]

As of February 1, 2005, the lowest rates MPC and MGC were charging Omega, an affiliated shipper, are shown in the following chart:[81]

Transportation Type/ Delivery Points	Firm	Firm	Interruptible
	Reservation per MDQ	Commodity Per Dt.	Commodity Per Dt.
MPC Delivery	$4.3181	$.1699	**$.1699**
MGC Delivery Except the Fort	$13.1766	**$.20**	**$.20**
MGC Delivery to the Fort	$18.10	**$.30**	$1.15

[79] Ex. 70, Tariff Sheet No. 5.

[80] The invoices collected in Ex. 67-D state on their face that they are for services provided beginning in February 2004. However, these are recreated invoices and they contain an incorrect date. Other evidence indicates Omega did not resume supplying gas to Fort Leonard Wood until February 2005, and MPC and MGC do not dispute the assertion that the dates on the recreated invoices are incorrect. Therefore, the Commission finds that the invoices in question are for the period after February 1, 2005.

[81] The chart is taken from Schallenberg Direct, Ex. 19, Page 26, Line 5.

On May 1, 2005, MPC and MGC gave an additional transportation discount to Omega for service provided to another bundled service customer. This time the customer was Emhart Glass Manufacturing, Inc. Omega had entered into a firm Natural Gas Sales Agreement with Emhart Glass beginning on December 1, 2004.[82] This was a firm contract and thus would ordinarily include a reservation charge. However, beginning on May 1, 2005, the invoices do not include a reservation charge, indicating that MPC and MGC waived that reservation charge for Omega's delivery of gas to Emhart Glass. On May 1, 2005, MGC was still charging Omega the maximum commodity rate under its tariff. That changed as of June 1, 2005, when the commodity rate for gas transported to Emhart Glass was reduced to $.30/Dth, the rate previously set for service to Fort Leonard Wood.[83]

As of May 1, 2005, the lowest rates MPC and MGC were charging Omega, an affiliated shipper, are shown in the following chart:[84]

Transportation Type/ Delivery Points	Firm	Firm	Interruptible
	Reservation per MDQ	Commodity Per Dt.	Commodity Per Dt.
MPC Delivery	**$0.00**	$.1699	**$.1699**
MGC Delivery Except the Fort	**$0.00**	**$.20**	**$.20**
MGC Delivery to the Fort	$18.10	**$.30**	$1.15

[82] Ex. 45.

[83] Ex. 67-D, Appendix D-17.

[84] The chart is taken from Schallenberg Direct, Ex. 19, Page 27, Line 1.

Conclusions of Law

1. The Firm Provisional Transportation Service, and Interruptible Provisional Transportation sections of MPC and MGC's tariffs contain provisions indicating as follows:

> 3.2 Range of Rates
>
> b. For all Transportation Agreements entered into by Transporter with any affiliate of Transporter after the effective date of tariff sheets having a Date of Issue of January 18, 1995, in those instances in which the term of the Agreement is greater than three (3) months:
>
> (1) The lowest transportation rate charged to an affiliate shall be the maximum rate that can be charged to non-affiliates. Any renegotiation or other type of modification to the rates of any then-effective Transportation Agreement is to be considered an applicable Transportation Agreement for the purpose of setting this maximum rate for non-affiliates.
>
> (2) Transporter will submit each such Transportation Agreement for Commission approval in those instances in which the rate offered to a non-affiliate is proposed to be greater than any rate offered to any affiliate.
>
> (3) Transporter will submit a rate comparison for all Transportation Agreements.
>
> (4) Rate comparisons for compliance with these provisions will be calculated assuming a 25% load factor.
>
> (5) These provisions will be applied to the Transporter's service area and the service area of Missouri Pipeline Company [Missouri Gas Company] as separate entities and on a separate basis.
>
> c. If at some point in time the Staff of the Commission determines that the provisions of Section 3.2(b) and Section 12(c) of the General Terms and Conditions are not effective in preventing rate discrimination to non-affiliates, after contacting Transporter, the Staff may file a notice to that effect with the Commission. As a consequence, on the date of such notice filing, said provisions will be terminated and at that point in time the following provisions will automatically replace Section 3.2(b) and Section 12(c) of the General Terms and Conditions with regard to all Transportation Agreements in effect at the time of Staff's filing of said notice with the Commission:
>
> The transportation rate charged to any affiliate on the Transporter's pipeline pursuant to a Transportation Agreement for a term greater than three (3) months entered into after January 5, 1995 shall be the maximum rate which may be charged to non-affiliates.[85]

[85] Ex. 70, Tariff Sheet Nos. 6-7 and 16-17, Ex. 71, Tariff Sheet Nos. 5-6 and 16-17. The Commission

From July 1, 2003, when MPC and MGC offered their first transportation rate discount to Omega, until June 1, 2006, when Omega was sold to an unaffiliated entity, Omega was affiliated with the pipeline companies and was an "Affiliate of Transporter" within the meaning of this tariff provision. Therefore, by terms of tariff provision 3.2b(1), the lowest transportation rate MGC and MPC offered to Omega is the maximum rate they can charge to a non-affiliated shipper.

2. Section 3.2(c) of those tariffs, as quoted in the previous paragraph, specifies that if Staff determines that the provisions of Section 3.2(b) and Section 12(c)[86] of the General Terms and Conditions Section of the tariffs are "not effective in preventing rate discrimination to non-affiliates", it may, "after contacting Transporter, … file a notice to that effect with the Commission." Once Staff files its notice, Sections 3.2(b) and Section 12(c) are to be automatically replaced with a revised tariff provision that simply states that "[t]he transportation rate charged to any affiliate on the Transporter's pipeline . . . shall be the maximum rate which may be charged to non-affiliates."

3. MPC and MGC contend the lower tariff rates charged to affiliates would not become the effective rate charged to non-affiliates until after Staff issues the notice to the Commission described in tariff section 3.2c. However, that reading of the tariff would not allow all aspects of the tariff to given their appropriate meaning. The Commission concludes that the correct interpretation of these tariff provisions is that section 3.2b(1) establishes that the lowest rate charged to an affiliated shipper is the highest rate that can

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required MPC and MGC to include these provisions in their tariffs as a condition for approving the transfer of those companies to UtiliCorp in 1994. *See, In the Matter of the Joint Application of Missouri Gas Company, Missouri Pipeline Company, and UtiliCorp United, Inc.*, Report and Order on Rehearing, 3 Mo. P.S.C. 236 (1994).

[86] Section 12.c requires the Transporter to supply a list of discounts offered to affiliated entities.

be charged to non-affiliated shippers. Subsections 3.2b (2)-(5) of that section then establish a procedure by which MPC or MGC could obtain an exception to that rule by requesting Commission approval of specific agreements that would allow for the charging of a lower rate to an affiliated shipper. The purpose of section 3.2c is to allow Staff to eliminate the possibility that MPC or MGC could obtain an exception to the general rule by eliminating subsections (2)-(5) if Staff finds that MPC and MGC are abusing that exception process. In other words, if Staff brings 3.2c into effect by giving notice to the Commission, the requirement that the lowest rate charged to an affiliated shipper becomes the highest rate that can be charged to a non-affiliated shipper becomes absolute, with no possible exceptions.

4. A tariff that has been approved by this Commission becomes Missouri law, with the same force and effect as a statute directly prescribed by the legislature. For that reason, tariffs are to be interpreted in the same manner as a statute.[87] One principle of statutory construction holds that the legislature is presumed to intend that "every word, clause, sentence, and provision of a statute have effect. Conversely, a presumption exists that the legislature does not insert idle verbiage or superfluous language in the statute."[88] Applying that rule of construction to its interpretation of the tariff, the Commission must presume that section 3.2c was intended to have some meaning. The foregoing interpretation provides a reasonable meaning for that provision.

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[87] *State ex rel. Laclede Gas Co. v. Pub. Serv. Comm'n,* 156 S.W.3d 513, 521 (Mo. App. W.D. 2005).

[88] *Cook v. Newman*, 142 S.W.3d 880, 892 (Mo. App. W.D. 2004).

5. Missouri's courts have held that "[t]he Commission has no jurisdiction to promulgate an order requiring a pecuniary reparation or refund."[89] Therefore, the Commission cannot order MGC or MPC to make any refund to its customers. If any customer of MGC or MPC seeks such a refund, they will need to file an appropriate petition in circuit court.

6. MPC and MGC argue that the Commission cannot adjust their rates in this case because the Commission has not considered all relevant factors, including operating expenses and the utility's rate of return. The Commission is required to consider those factors in setting rates for a utility.[90] However, this is not a rate case and the Commission is not attempting to determine an appropriate rate for the companies. Rather, the Commission is simply considering Staff's complaint and determining the applicability of a provision contained in MPC and MGC's tariffs. Simply put, the Commission is acting to enforce an existing tariff rather than exercising its ratemaking authority.

Decision

Did MPC and MGC provide transportation service to its affiliate, Omega, at a discounted rate, and if so, should this rate become the maximum rate that MPC and MGC could charge any of its non-affiliated customers for similar services?

The recreated invoices offered into evidence by Staff show the rate that MPC and MGC actually charged their affiliate, Omega, for transporting natural gas to Omega's gas marketing customers. Those invoices demonstrate that the pipeline companies offered discounted transportation rates to their affiliate. By the explicit terms of their tariffs, the

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[89] *DeMaranville v. Fee Fee Trunk Sewer, Inc.,* 573 S.W. 2d 674, 676 (Mo. App. E.D. 1978).

[90] *State ex rel. Util. Consumers Council of Mo., Inc. v. Pub. Serv. Comm'n,* 585 S.W. 2d 41, 49 (Mo banc. 1979)

lowest transportation rate MPC and MGC charged an affiliate is the maximum rate they can charge to a non-affiliate.

For MPC and MGC, those discounted rates, and the dates when the rates were first offered to an affiliate, are shown in the following chart:

Transportation Type/ Delivery Points	Firm	Firm	Interruptible
	Reservation per MDQ	Commodity Per Dt.	Commodity Per Dt.
MPC Delivery	**$0.00 beginning May 1, 2005**	$.1699	**$.1699 beginning September 1, 2003**
MGC Delivery Except the Fort	**$0.00 beginning May 1, 2005**	**$.20 beginning July 1, 2003**	**$.20 beginning September 1, 2003**
MGC Delivery to the Fort	$18.10	**$.30 beginning February 1, 2005**	$1.15

Count IV

Findings of Fact

The fourth count of Staff's complaint alleges that MPC and MGC violated their tariffs by failing to disclose the discounted transportation rates they gave to their affiliate, Omega. Section 12.c of the General Terms and Conditions section of MPC and MGC's tariffs require them to submit a quarterly report to Staff listing bids or offers they quote for transportation service rates where the bid is for less than the maximum rate established in the tariff. As part of the report, MGC and MPC are required to disclose whether the entity that would receive the discounted rate is an affiliate.[91] In the second and third quarters of 2003, MPC and MGC did not report the discounted rates that it gave to Omega.[92] Nor did it report giving a discount to any other entity, affiliated or not. The discounts that Staff says

[91] Ex. 70, Tariff Sheet No. 39, and Ex. 71, Tariff Sheet No. 39.

[92] Imhoff Direct, Ex. 1, Page 10, Lines 27-30.

MPC and MGC should have reported are the discounts for transportation of gas to the City of Cuba and G-P Gypsum discussed in detail regarding Count III of Staff's complaint. Regardless of whether those discounts were given to Cuba or to Omega, the recreated invoices offered into evidence by Staff demonstrate conclusively that MPC and MGC gave transportation discounts during that period.

MPC and MGC agree that they did not report the discounts described by Staff, but contend that they were under no obligation to report those transactions since the discounts were offered to the City of Cuba, which is not an affiliate.

Conclusions of Law

1. Section 12.c of the General Terms and Conditions section of MPC and MGC's tariffs states as follows:

> 12. Operation of Rate Schedule in Conjunction with Marketing Affiliates.
>
> . . .
>
> c. Transporter will submit to the Commission's Energy – Rates Staff once every three months, a list of all bids or offers Transporter quotes for transportation service rates for its pipeline where the bid is less than the Maximum Rate contained in this tariff for Transporter's area. Transporter will provide the bid price quoted, the length of and dates of all offerings, the name, address and telephone number of the party to whom the bid was given, any other terms of the bid and a rate comparison sheet for all bids and offers for each month. For each such bid or offering, Transporter will completely explain whether the entity being offered the rate is affiliated in any way with Transporter or with any of its affiliates. If the entity is affiliated, Transporter will completely explain such affiliation. Transporter will respond immediately to Staff inquiries concerning discounting.[93]

This tariff provision requires MPC and MGC to file a report any time they offer a discount to any shipper on their pipelines. It requires them to file additional information if the discount

[93] Ex. 70, Tariff Sheet No. 39, Ex. 71, Tariff Sheet No. 39.

is offered to an affiliate, but it requires the basic report to be filed regardless of whether an affiliate is involved.

Decision

Did MPC and MGC violate their tariffs by failing to report their offer of discounted transportation service to its affiliate, Omega, in its second quarter and third quarter 2003 reports to the Commission's Energy Staff?

The tariff provision in question is designed to allow Staff to monitor the affiliate transactions in which MPC and MGC might engage to ensure that such transactions are not abusive. The plain language of the tariff requires MPC and MGC to report all offered discounts to Staff in a quarterly report. All discounts must be reported, regardless of whether the discounts are offered to an affiliate. The recreated invoices conclusively show that MPC and MGC offered discounts to shippers on their pipelines in the second and third quarters of 2003. Those discounts were not reported to Staff, and thereby the tariff provision was violated. Staff proved count IV of its complaint.

<u>Count V</u>

Findings of Fact

The fifth count of Staff's complaint alleges that MGC violated its certificate of convenience and necessity by constructing a new lateral line off the pipeline to provide service to Willard Asphalt, a gas-marketing customer of Omega.

MGC was issued a certificate by the Commission in Case No. GA-90-280. In a subsequent case, in which the Commission authorized the sale of MPC and MGC to UtiliCorp, the Commission found that "the certificates issued, and which will be passed to UCU as the result of this purchase, are for the operation of a natural gas pipeline. This does not include the sale of gas, the by-pass of LDCs, or operation other than in the designated territory."[94] In other words, MGC holds a line certificate of convenience from the Commission allowing it to transport natural gas through a described corridor. It does not hold an area certificate that would authorize it to distribute gas to retail customers.

In 2004, MGC constructed a lateral extension from its pipeline to establish a new delivery point to provide gas service to Willard Asphalt. The lateral extension runs about 1400 feet from the pipeline to connect with the asphalt plant's gas system at a new meter station. The entire extension is located on Willard Asphalt's property.[95] Willard Asphalt entered into a Natural Gas Sales Agreement with Omega beginning on April 1, 2004.[96]

Staff also alleges that MGC violated its tariff by not requiring either Willard Asphalt or Omega to pay the cost of constructing that lateral line. MGC's tariff requires a shipper, in this case, either Willard Asphalt or Omega, to reimburse the pipeline for the cost of constructing facilities needed to deliver gas to the shipper.[97] The cost of constructing the lateral to serve Willard Asphalt is on MGC's books, and neither Willard Asphalt, nor Omega, has reimbursed MGC for those costs.[98]

MGC concedes that it paid the cost to construct the lateral but defends that cost as a prudent business decision. MGC indicates that it added a new delivery point to its pipeline to allow it to serve Willard Asphalt, and to create a second delivery point to aid the City of

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[94] Ex. 83, *In the Matter of the Joint Application of Missouri Gas Company, Missouri Pipeline Company, and UtiliCorp United, Inc.,* Report and Order, 3 Mo P.S.C. 3d 216, 223 (1994).

[95] Transcript, Page 669, Lines 17-25.

[96] Ex. 33.

[97] Ex. 70, Tariff Sheet No. 31, General Terms and Conditions Section 6.e.

[98] Schallenberg Direct, Ex. 19, Pages 35-36, Lines 25-27, 1-2, and Transcript, Page 334, Lines 24-25.

St. Robert in the expansion of its municipal gas system.[99] MGC also states that the construction of the lateral has substantially increased its revenues and has been a sound investment.[100] Furthermore, MGC has not filed a rate case since the lateral was constructed. As a result, the cost of constructing the lateral is not reflected in MGC's current rates.

Conclusions of Law

27. Section 6.e of the General Terms and Conditions section of MGC's tariff states as follows:

> 6. Statements and Payments.
>
> e. Shipper will reimburse Transporter or cause Transporter to be reimbursed for any and all costs and expenses incurred in constructing, establishing or modifying the facilities required for receipt and/or delivery of gas hereunder. Upon request, an estimate shall be provided in writing to the Shipper with a breakdown showing at least the major cost components. Shipper shall be responsible for reimbursing Transporter for only the actual costs incurred by Transporter in constructing, establishing or modifying the facilities required for receipt and/or delivery of gas hereunder.

Decision

Did MGC construct a lateral line for a certain industrial customer to benefit its affiliate, Omega, without demanding reimbursement from either Omega or the customer, in violation of its tariff or its certificate?

Staff established that MGC constructed a short, 1400 foot, line from its main pipeline to establish a connection to serve an industrial customer. MGC can establish a new connection point on its pipeline without violating its line certificate, but at some point, an

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[99] Ries Rebuttal, Ex. 304, Page 42, Lines 8-14.

[100] Id. at Page 43, Lines 6-18.

authorized new connection becomes long enough to constitute a new lateral line that would require a revised certificate. Staff did not present sufficient evidence to establish that this new connection required a revised certificate and that its construction violated MGC's existing certificate of convenience and necessity. Staff has the burden of proving its complaint and it has failed to meet that burden with regard to this aspect of Count V.

The other aspect of Count V alleges MGC violated its tariff by failing to demand reimbursement from the shipper for the cost of constructing the lateral line. MGC's tariff requires the shipper to reimburse MGC for those costs and MGC apparently has not attempted to collect that reimbursement, instead carrying those costs on its own books. Therefore, MGC has violated its tariff.

So far, however, MGC's decision not to seek reimbursement of those costs has not had any impact on its customers. Those costs have not been included in the calculation of MGC's costs for purposes of establishing rates because MGC's rates have not been adjusted since those costs were incurred. MGC's decision not to seek reimbursement of these costs may become important in a future rate case, but it is of no importance now. As a result, there is no need for Staff to seek penalties against MGC for this violation of its tariff.

Count VI

Staff's complaint originally contained a sixth count alleging that MPC and MGC violated their tariffs by providing preferential terms of payment to Omega. In his surrebuttal testimony, Bob Schallenberg indicated that Staff is no longer seeking relief on this count.[101]

[101] Schallenberg Surrebuttal, Ex. 67, Page 1, Lines 17-22.

Since Staff is no longer seeking relief under this count, the Commission will not address it further.

GENERAL CONCLUSIONS OF LAW

The Missouri Public Service Commission has reached the following conclusions of law that are applicable to all counts of Staff's complaint:

1. MPC and MGC are "Gas Corporations" and "Public Utilities," as those terms are defined at Section 386.020 (18) and (42), RSMo Supp. 2006. As such, they are subject to regulation by this Commission.

2. Section 393.140(1), RSMo 2000 gives the Commission general supervisory authority over all Missouri gas corporations.

3. Section 393.140(11), RSMo 2000 gives the Commission the power to require every gas corporation to file and maintain public tariffs describing the rates it will charge, as well as the terms under which it will offer service to the public. That section also requires a gas corporation to comply with the terms of its own tariff.

4. A tariff that has been approved by the Commission becomes Missouri law, with "the same force and effect as a statute directly prescribed from the legislature."[102]

5. MPC and MGC are obligated to comply with the provision of their own tariffs.

6. Section 386.390.1, RSMo 2000, authorizes the Commission to bring a complaint against a public utility on its own motion.

7. As the party bringing a complaint, Staff has the burden of proving its allegations.[103]

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[102] *State ex rel. Laclede Gas Co. v. Pub. Serv. Comm'n,* 156 S.W. 3d 513, 521, (Mo. App. W.D. 2005)

[103] *State ex rel. GS Technologies Operating Co., Inc. v. Pub. Serv. Comm'n*, 116 S.W.3d 680 (Mo. App. W.D. 2003).

8. Section 386.570.1, RSMo 2000 provides that any public utility that fails to comply with any provision of law, or with any "order, decision, decree, rule, direction, demand or requirement" of the Commission "is subject to a penalty of not less than one hundred dollars nor more than two thousand dollars for each offense."

9. The General Counsel of the Commission is authorized by Section 386.600, RSMo 2000, to bring an action in circuit court to recover a penalty against a public utility.

IT IS ORDERED THAT:

1. Staff proved the allegations contained in Count I of its complaint. The Commission's General Counsel is authorized, pursuant to Section 386.600, RSMo 2000, to file a petition in the circuit court of his choosing to seek any applicable penalties against Missouri Pipeline Company and Missouri Gas Company.

2. Staff failed to prove the allegations contained in Count II of its complaint and relief on that Count is denied.

3. Staff proved the allegations contained in Count III of its complaint. By the terms of their tariffs, the rates Missouri Pipeline Company and Missouri Gas charged to an affiliated shipper became the maximum rate that could be charged to a non-affiliated shipper, as indicated in the following chart:

Transportation Type/ Delivery Points	Firm	Firm	Interruptible
	Reservation per MDQ	Commodity Per Dt.	Commodity Per Dt.
MPC Delivery	**$0.00 beginning May 1, 2005**	$.1699	**$.1699 beginning September 1, 2003**
MGC Delivery Except the Fort	**$0.00 beginning May 1, 2005**	**$.20 beginning July 1, 2003**	**$.20 beginning September 1, 2003**
MGC Delivery to the Fort	$18.10	**$.30 beginning February 1, 2005**	$1.15

4. Staff proved the allegations contained in Count IV of its complaint. The Commission's General Counsel is authorized, pursuant to Section 386.600, RSMo 2000, to file a petition in the circuit court of his choosing to seek any applicable penalties against Missouri Pipeline Company and Missouri Gas Company.

5. With regard to Count V of its complaint, Staff failed to prove that MGC violated its certificate of convenience and necessity. Staff proved that MGC violated its tariff but relief for that violation is denied.

6. Staff's Motion for Sanctions for Destruction of Documents is denied except for the adverse evidentiary inferences explained in the body of this Report and Order.

7. Respondents' Motion to Supplement Exhibit 311 is denied.

8. This Report and Order shall become effective on October 21, 2007.

BY THE COMMISSION

Colleen M. Dale
Secretary

(S E A L)

Davis, Chm., Clayton, Appling, Jarrett, CC., concur;
Murray, C., dissents
and certify compliance with the provisions
of Section 536.080, RSMo 2000.

Dated at Jefferson City, Missouri,
on this 11th day of October, 2007.