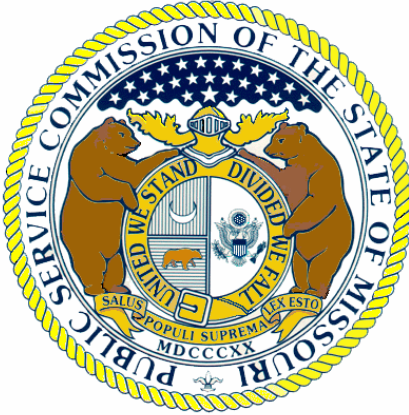


**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**



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, Operate, Control,)
Manage, and Maintain a Natural Gas Distribution System)
to Provide Gas Service in Lebanon, Missouri.)

Case No. GA-2007-0212,
et al.

REPORT AND ORDER

Issue Date: **August 16, 2007**

Effective Date: **August 26, 2007**

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE 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) **Case No. GA-2007-0212,**
Authorizing It to Construct, Install, Own, Operate, Control,) **et al.**
Manage, and Maintain a Natural Gas Distribution System)
to Provide Gas Service in Lebanon, Missouri.)

APPEARANCES

James M. Fischer, Fischer & Dority, P.C., 101 Madison Street, Suite 400, Jefferson City, Missouri 65101, for Southern Missouri Gas Company, d/b/a Southern Missouri Natural Gas.

Khristine A. Heisinger and **Charles Hatfield**, STINSON MORRISON HECKER LLP, 230 West McCarty Street, Jefferson City, Missouri 65101, for Missouri Propane Gas Association.

Marc D. Poston, Senior Public Counsel, Office of the Public Counsel, Post Office Box 2230, Jefferson City, Missouri, for the Office of the Public Counsel and the public.

Kevin A. Thompson, General Counsel, Missouri Public Service Commission, Post Office Box 360, Jefferson City, Missouri 65102, for the Staff of the Missouri Public Service Commission.

REGULATORY LAW JUDGE: Nancy Dippell, Deputy Chief.

REPORT AND ORDER

Syllabus: This Report and Order grants Southern Missouri Gas Company, L.P., d/b/a Southern Missouri Natural Gas, a certificate of convenience and necessity for a natural gas distribution system to provide gas service in Houston, Licking, and Lebanon, Missouri, conditioned on the approval of its financing application and that the shareholders, not the ratepayers, bear the risk of any loss caused by failure to meet the conversion projections.

Procedural History

On December 6, 2006, Southern Missouri Gas Company, L.P., d/b/a Southern Missouri Natural Gas, filed an application for a certificate of convenience and necessity to provide natural gas distribution service to the City of Lebanon, Missouri.¹ On December 12, 2006, Southern Missouri Gas filed an application for approval to issue approximately \$10 million in equity capital and \$50 million in notes and other indebtedness in order to finance the proposed expansion of its system.² On February 15, 2007, Southern Missouri Gas filed an application for a certificate of convenience and necessity to provide natural gas service in Houston, Licking, and Mountain View, Missouri.³ Southern Missouri Gas later withdrew its request to serve Mountain View.⁴

The Missouri Propane Gas Association and Southern Star Gas Pipeline, Inc., were each granted intervention. The three cases were consolidated at the request of Southern Missouri Gas and without objection by the other parties.

The MPGA filed a Motion to Dismiss or in the Alternative to Stay Proceedings pending the outcome of a municipal election set for August 7, 2007, regarding the franchise in Lebanon, Missouri. That motion was denied by the Commission.

The Staff of the Missouri Public Service Commission filed its recommendation on June 13, 2007. Staff recommended conditionally granting the certificates but withholding approval of the financing application until Staff has reviewed the final terms and conditions. Staff intends to file an additional recommendation in the financing case. Southern Missouri

¹ Case No. GA-2007-0212.

² Case No. GF-2007-0215.

³ Case No. GA-2007-0310.

⁴ *Response of Southern Missouri Natural Gas to the Staff Recommendation*, p. 2 (filed June 13, 2007).

Gas responded that it agreed with Staff's recommendations and the issuance of a conditional certificate.

An evidentiary hearing was held on July 27, 2007, with all parties being present except Southern Star. Southern Missouri Gas presented two witnesses, Randy Maffett and Joe Knapp. The MPGA presented one witness, Ed Simmons. And, Staff presented two witnesses, Tom Solt and David Murray. The Commission received 16 exhibits into evidence.

On August 10, 2007, a Notice of Election Results was filed. The Commission notified the parties that it intended to take official notice of the election results and no party objected. Therefore, the Commission hereby takes official notice of the election results of the August 7, 2007, election in the City of Lebanon, Missouri.

Briefs were filed on August 13, 2007. Southern Star did not participate in this matter after it was granted intervention.

Findings of Fact

The Missouri Public Service Commission, having considered all of the competent and substantial evidence upon the whole record, makes the following findings of fact:

1. Southern Missouri Gas is a Missouri limited partnership with its primary business address at: 301 E. 17th Street, Mountain Grove, Missouri 65711.
2. Southern Missouri Gas "owns and operates a natural gas transmission and distribution system located in southern Missouri which serves approximately 7,500 residential, commercial and industrial customers."⁵

⁵ Exhibit 2, para. 1.

3. Approximately 6,800 of Southern Missouri Gas's current customers are residential customers.⁶

4. Southern Missouri Gas is the successor to Tartan Energy Company, L.C., d/b/a Southern Missouri Gas Company, L.C., which was granted a certificate of convenience and necessity to construct and operate a natural gas distribution system in several municipalities, including Houston and Licking, Missouri, in the spring of 1995.⁷

5. In the GA-94-127 Report and Order, Tartan Energy was found to be financially and technically qualified to provide natural gas service. The Commission also determined that it was in the public interest for Tartan Energy to be granted a certificate of convenience and necessity in ten communities, including Houston and Licking.⁸

6. A trunkline and distribution facilities authorized in Case No. GA-94-127 was constructed; however, Southern Missouri Gas did not complete the trunkline and distribution systems in Houston and Licking.⁹

7. Southern Missouri Gas currently serves the communities of Rogersville, Marshfield, Ava, Norwood, Mountain Grove, West Plains, Willow Springs, Cabool, and Mansfield.¹⁰

⁶ Transcript, p. 70, lines 16-18.

⁷ See, Case No. GA-94-127, Order Approving Tariffs and Authorizing the Commencement of Construction of Gas Facilities (issued April 14, 1995), and Order Granting Certificate of Convenience and Necessity for Mountain View, Missouri, and Authorizing Construction of Distribution Facilities in Mountain View, Missouri, and in Texas and Wright Counties (issued May 19, 1995).

⁸ *Report and Order, In re Application of Tartan Energy Company, L.C., d/b/a Southern Missouri Gas Company, for a Certificate of Convenience and Necessity*, Case No. GA-94-127, 3 Mo. P.S.C. 3d 173 (September 16, 1994).

⁹ Ex. 5, para. 4.

¹⁰ Tr. p. 73, lines 21-23.

8. Southern Missouri Gas is owned by Sendero SMGC GP Acquisition Company, LLC (2%), and Sendero SMGC Limited Acquisition Company, LLC (98%). Southern Missouri Gas is the only asset owned by these two entities. Sendero SMGC GP Acquisition Company, LLC, and Sendero SMGC Limited Acquisition Company, LLC, are owned by Sendero Capital Partners Missouri, LLC (4.5590%), CHx Capital Missouri, Inc. (93.0639%), and Michael J. Lewis (2.3771%). Randy Maffett owns Sendero Capital Partners Missouri, LLC, and Alex Cranberg owns CHx Capital Missouri, Inc.¹¹

9. Sendero SMGC GP Acquisition Company, LLC, and Sendero SMGC Limited Acquisition Company, LLC, have no assets other than their interests in Southern Missouri Gas.¹²

10. Southern Missouri Gas has a management agreement with Sendero Asset Management, LLC, for which Southern Missouri Gas compensates Sendero Asset Management approximately \$200,000 annually.¹³

11. The ownership of Southern Missouri Gas has been in its current structure since 2005.¹⁴

12. The ownership structure set out in Exhibit 10 will change with the addition of investors through the proposed financing; however, the final ownership structure is not yet known.¹⁵

¹¹ Ex. 10; Tr. p. 77, lines 4-8; and, Tr. p. 131, lines 4-9 and 17-19.

¹² Tr. p. 77, lines 9-24, and p. 78, lines 15-24.

¹³ Tr. p. 77, line 25, through p. 78, line 9.

¹⁴ Tr. p. 42, line 20.

¹⁵ Tr. p. 134, line 5 through p. 135, line 19.

13. In the first two years, the current owners have reinvested \$1.5 million into the Company and have not taken any distributions out of the Company.¹⁶

14. Southern Missouri Gas has been prohibited by its current lender from taking any distributions for at least three years.¹⁷

15. On December 6, 2006, Southern Missouri Gas filed an Application requesting a certificate of convenience and necessity for a local distribution system serving Lebanon, Missouri.¹⁸

16. On December 12, 2006, Southern Missouri Gas filed an application for approval to issue approximately \$10 million in equity capital and \$50 million in notes and other indebtedness in order to finance the proposed expansion of its system.¹⁹

17. On February 15, 2007, Southern Missouri Gas filed an application for a certificate of convenience and necessity to provide natural gas service in Houston, Licking, and Mountain View, Missouri.²⁰

18. Southern Missouri Gas later withdrew its request to serve Mountain View.²¹

19. Attached to the Application in Case No. GA-2007-0212 was a map depicting the service territory requested to be included in the certificate of convenience and

¹⁶ Tr. p. 137, line 22, through p. 138, line 5.

¹⁷ Tr. p. 295, lines 8-12.

¹⁸ Ex. 2.

¹⁹ Ex. 7, para. 4..

²⁰ Ex. 5.

²¹ *Response of Southern Missouri Natural Gas to the Staff Recommendation*, p. 2 (filed June 13, 2007).

necessity.²² The Application in Case No. GA-2007-0310 also included by reference the map attached to an earlier application for a certificate in the Houston and Licking areas.²³

20. The maps consisted of line drawings with the city locations noted and, in the case of the Houston and Licking map, the mileage between points was also included.

21. More detailed maps were submitted to the Staff but not filed in the official case file.²⁴

22. No party claimed any prejudice or harm due to the quality of the maps Southern Missouri Gas filed with its applications.

23. The certificate applications also included either an attached list of metes and bounds descriptions²⁵ or a reference to a metes-and-bounds description.²⁶

24. The metes and bounds descriptions in conjunction with the maps provide sufficient information for a Commission determination of the proposed service territory.

25. Each of the certificate applications included a financial feasibility study for the proposed expansion.²⁷

26. The Application in GA-2007-0212 included a list of ten persons residing in or who are landowners within the proposed Lebanon service area.²⁸

²² Ex. 2, Appendix B.

²³ Ex. 5, p. 3 (referencing Case No. GA-94-127).

²⁴ Tr. p. 267, line 11.

²⁵ Ex. 2, Appendix C.

²⁶ Ex. 5, p. 3 (referencing Case No. GA-94-127).

²⁷ Ex. 4P and Ex. 6HC.

²⁸ Ex. 2, Appendix E.

27. The Application in GA-2007-0310 included a reference to a list of ten persons residing in or who are landowners within the proposed Licking and Houston service areas.²⁹

28. The Cities of Houston and Licking have granted a natural gas franchise to Southern Missouri Gas.³⁰

29. The Council of the City of Lebanon passed an ordinance granting Southern Missouri Gas a natural gas franchise on January 16, 2007.³¹

30. Each of the franchise agreements gives the respective cities the option to purchase the distribution system within it for the net book value plus 15%.³²

31. None of the franchise agreements were exclusive.³³

32. On August 7, 2007, the City of Lebanon held an election at which the citizens of the municipality overwhelmingly voted to grant Southern Missouri Gas a natural gas franchise.³⁴

33. State and county road right-of-way agreements have also been granted in areas where the distribution pipes will be laid.³⁵

34. Southern Missouri Gas proposes to use its current tariff rates and regulations for natural gas service in the expanded areas.³⁶

²⁹ Ex. 5, referencing Case No. GA-94-127.

³⁰ Ex. 5, Appendix D.

³¹ Ex. 3.

³² Ex. 5, Appendix D, and Ex. 3.

³³ Ex. 5, Appendix D, and Ex. 3.

³⁴ *Notice of Election Results*, filed August 10, 2007.

³⁵ Tr. p. 143.

³⁶ Ex. 2, para. 9, and Ex. 5, para. 8.

35. Attached to the Application in Case No. GF-2007-0215 was a financing plan in accordance with Commission rules. The financing plan included a description of the expected rates, terms and conditions for the debt securities, as well as a pro-forma balance sheet and income statement “showing the effect of the issuance of the equity capital and the debt securities” on the company.³⁷

36. The financing application also contained a five-year capital expenditure schedule.³⁸

37. The financing arrangement is expected to increase Southern Missouri Gas’s working capital credit line to \$25 million.³⁹

38. The increase in working capital will improve the Company’s working capital structure.⁴⁰

39. Natural gas distribution companies need large amounts of working capital because of the delay between the purchase of natural gas and receipt of payment from the ultimate consumer.⁴¹

40. The equity investors will be one or more of “three large accredited institutional investors, all of whom are experienced in the energy and specifically the natural gas and distribution businesses.”⁴²

³⁷ Ex. 7, para. 7; and Ex. 8P.

³⁸ Ex. 7, Appendix E.

³⁹ Ex. 8; Tr. p. 296, lines 15-21.

⁴⁰ Tr. pp. 298-299.

⁴¹ Tr. p. 150, line 17, through p. 151, line 2; and Tr. p. 295, line 18, through p. 297, line 4.

⁴² Tr. p. 66, lines 16-19; Ex. 19, p. 3.

41. Southern Missouri Gas is currently still engaged in negotiations with potential investors and, once its negotiations are complete, will file an amendment to its financing application with supporting documentation.⁴³ The exact terms and conditions of the proposed financing will not be known until that time.⁴⁴

42. Having regulatory approval of the expanded certificate will aid Southern Missouri Gas in obtaining the financing.⁴⁵

43. Southern Missouri Gas will not be able to complete the proposed expansion to Lebanon, Houston, and Licking without obtaining financing.⁴⁶

44. Even though Southern Missouri Gas is in the final stages of negotiations, it has no commitments for financing.⁴⁷

45. Staff recommended granting the certificate conditioned on the financing being approved. Staff will make a recommendation regarding the financing application as soon as possible after the final terms and conditions are made available to Staff.⁴⁸

46. Staff expressed concerns about the valuation of the Company in its audited financial statements as compared with its annual reports. Staff's concern is that the potential investors understand the proper valuation of the Company.⁴⁹

⁴³ Tr. pp. 66-67.

⁴⁴ Tr. p. 290.

⁴⁵ Ex. 5, para. 13; and Tr. p. 140.

⁴⁶ Tr. p. 90, lines 11-14.

⁴⁷ Tr. p. 91, lines 12-22.

⁴⁸ Ex. 19.

⁴⁹ Ex. 19; and Tr. pp. 274-279.

47. The feasibility studies include engineering cost estimates, estimates of system demand, plans for financing, revenues and expenses during the first ten years of operation, and proposed rates and charges.⁵⁰

48. The inputs to the feasibility studies included: estimated household data based upon federal census data, conversion to natural gas of various types of existing customers, various costs associated with providing service to existing and new areas, proposed capital expenditures, and other assumptions.”⁵¹

49. The feasibility studies also contain a sensitivity analysis of the total projected demand for natural gas which was estimated to be 50%⁵² of the current households that Southern Missouri Gas determined currently use propane gas.

50. It has been Southern Missouri Gas’s experience in similar communities in the area that approximately 52% of propane-using households will convert to natural gas over a five-year period after it becomes available.⁵³

51. The number of households currently using propane was determined by counting propane tanks during a visual walk through of the area.⁵⁴

52. Based on Southern Missouri Gas’s experience, about 20% to 30% of all-electric households will convert to natural gas.⁵⁵

⁵⁰ Ex. 4P; Ex. 6HC.

⁵¹ Ex. 19, p. 2.

⁵² Mr. Maffett testified that the actual “take rate” for Southern Missouri Gas was 52% but the number was rounded for ease of use and to assure a conservative estimate. Tr. pp. 61 and 97.

⁵³ Tr. p. 61.

⁵⁴ Tr. p. 88.

⁵⁵ Tr. p. 61.

53. In the event that the expected conversion rate is not achieved, Southern Missouri Gas shareholders expect to absorb the loss instead of the ratepayers.⁵⁶

54. New developments are expected to have a higher “take rate” than in the older neighborhoods where conversion from propane or electricity to natural gas might be required.⁵⁷

55. After the first five years, Southern Missouri Gas expects growth of 1.5% to 2.0% annually.⁵⁸

56. In addition to its review of the Company’s inputs, “Staff analyzed the effects of various changes to the assumptions, substituting more conservative estimates in place of some of the Company’s inputs. Staff made the following adjustments to the Company’s model: growth rates were replaced by the Company’s actual growth experienced on the existing system from 1995 to 2000; Staff removed all gas sales revenue and expense; added inflation during 2007 for the current SMNG system; tripled the distribution cost per customer from \$500 to \$1,500; added an allowance for interest on working capital; and doubled the estimated pipeline cost from \$9,750,000 to \$19,500,000.”⁵⁹

57. Staff evaluated the feasibility of these projects “by looking at the internal rate of return (IRR) for the project over the twenty (20) years covered by the model plus a terminal value. A hurdle rate of ten percent (10%) was considered to be the break point for feasibility. The IRR produced in the model, as adjusted by Staff, is thirteen percent

⁵⁶ Tr. pp. 75-76.

⁵⁷ Tr. pp. 123-124.

⁵⁸ Tr. p. 152, line 4.

⁵⁹ Ex. 19, p. 2.

(13%).⁶⁰ The model, using the numbers submitted by Southern Missouri Gas, produced an IRR of 41%.⁶¹

58. Staff's conclusion was that even with the more conservative inputs the expansion project is economically feasible, though not completely without risk.⁶²

59. One risk identified by Staff is that the customer conversion rate from propane to natural gas will be affected by entrenched competition from propane dealers, whose prices and business practices are unregulated.⁶³

60. There are no regulated gas suppliers in the areas where expansion of the certificate is requested.⁶⁴

61. The propane gas market is very competitive in Lebanon. There are seven propane dealers in the city and five or six others in the surrounding area.⁶⁵

62. Using information from the Energy Information Administration, the residential price per gallon of propane on March 12, 2007, was \$1.68, which equates to an equivalent price per Ccf of natural gas of \$1.83.⁶⁶

63. The purchased gas adjustment (PGA) rate for Southern Missouri Gas in March was \$0.95 per Ccf. Since the price of propane is a delivered price, Staff calculated the delivered price of 1,000 Ccf of natural gas to compare with the equivalent of 1,000 Ccf of propane. This was done by adding the commodity charge of \$0.357 and the customer

⁶⁰ Ex. 19, p. 3.

⁶¹ Ex. 19, p. 3.

⁶² Ex. 19, p. 3; and Tr. p. 251.

⁶³ Tr. p. 248 lines 5-13.

⁶⁴ Ex. 2, para. 10, and Ex. 5, para. 9.

⁶⁵ Tr. p. 206, lines 11-14.

⁶⁶ Ex. 19, p. 3.

charge of \$0.12 to the price per Ccf of natural gas. The customer charge equivalent was determined by dividing the \$120.00 customer charge for 12 months by 1,000. The cost of 1,000 Ccf of natural gas, calculated this way, would be \$1,427, whereas the price of 1,000 Ccf of propane would be \$1,834.⁶⁷

64. The price of propane would have to drop to approximately \$1.307 per gallon to be competitive with natural gas.⁶⁸

65. Per MMBTU, Southern Missouri Gas can deliver natural gas for about \$13.00 compared to about \$20.00 per MMBTU for propane.⁶⁹

66. Natural gas is cheaper for heating than propane,⁷⁰ and cost-competitive with electricity and fuel oil.⁷¹

67. Because propane is not regulated, propane dealers have more flexibility than natural gas distributors in setting prices.⁷²

68. The availability of natural gas would allow energy consumers in Lebanon, Houston, and Licking to reduce their energy costs.⁷³

69. The availability of natural gas in Lebanon, Houston and Licking would create competition with other energy providers that could drive energy prices down for all customers.⁷⁴

⁶⁷ Ex. 19, p. 3.

⁶⁸ Ex. 19, p. 3.

⁶⁹ Tr. pp. 62-63.

⁷⁰ Tr. p. 62.

⁷¹ Tr. p. 63, lines 6-9.

⁷² Tr. 101, lines 7-17.

⁷³ Tr. p. 58, line 17, through p. 59, line 3, and p. 109, lines 7-14.

⁷⁴ Tr. pp. 108-109.

70. Authorizing Southern Missouri Gas to provide natural gas service will benefit the public by offering another choice of energy providers, increasing “operational convenience,” and potentially decreasing energy costs.⁷⁵

71. If businesses reduce their energy costs, they may also reduce their retail costs or add employees.⁷⁶

72. Joe Knapp is the City Administrator for Lebanon. His duties include economic development for that city.⁷⁷ Mr. Knapp testified that creation of a competitive energy market in Lebanon would result in the creation of jobs in the community.⁷⁸

73. Mr. Knapp identified three instances where economic development opportunities were lost when new businesses failed to consider Lebanon a viable alternative because of the lack of available natural gas.⁷⁹

74. Mr. Knapp estimated the combined impact of these lost opportunities was 200 additional jobs and \$180 million of capital investment into the Lebanon community.⁸⁰

75. The cost of municipally supplied electricity in Lebanon is expected to increase by 30% to 40% in the future.⁸¹

76. Lebanon is a manufacturing community, with approximately 6,000 industrial jobs. The manufacturers in Lebanon include Emerson, Durham, Carr Industries, DTE Metal

⁷⁵ Tr. pp. 58-59.

⁷⁶ Tr. p. 163, lines 2-8.

⁷⁷ Tr. p. 178, line 14, through p. 179, line 15.

⁷⁸ Tr. p. 180, lines 5-12.

⁷⁹ Tr. pp. 180-81.

⁸⁰ Tr. p. 181.

⁸¹ Tr. p. 183, lines 16-22.

Products, Precision, Bass Tracker, Landau Boats, and G3 Boats. Another large employer in the area is St. John's Hospital.⁸²

77. Mr. Knapp testified that the availability of natural gas would help Lebanon attract new industry because natural gas availability is often requested by prospective employers.⁸³

78. Existing industries in Lebanon have also requested that the City of Lebanon seek out natural gas service.⁸⁴

79. The City of Lebanon issued requests for proposals (RFPs) to 20 natural gas suppliers and received two bids. Southern Missouri Gas was the winning bidder.⁸⁵

80. The addition of natural gas service in the City of Lebanon will result in the creation of jobs in the community by allowing the city to attract new industries and aiding its existing industrial base.⁸⁶

81. The City of Lebanon originally passed an ordinance authorizing a natural gas franchise in the 1960s but no natural gas service to the city was constructed.⁸⁷

82. The total number of households is approximately 6,000 in Lebanon, and 1,000 each in Houston and Licking.⁸⁸

⁸² Tr. p. 199, lines 8-16.

⁸³ Tr. pp. 180-81.

⁸⁴ Tr. p. 184.

⁸⁵ Tr. pp. 173-74, 186-187.

⁸⁶ Tr. pp. 180-81, 184.

⁸⁷ Tr. p. 182.

⁸⁸ Tr. p. 61.

83. There is a public need for natural gas and transportation service in Lebanon.⁸⁹

84. Members of the MPGA have propane gas customers in Missouri Southern Gas's proposed service territory.⁹⁰ Peak-shaving plants and standby plants are propane-based facilities used in areas where natural gas pressure is inadequate in peak usage periods. Such facilities are used in Springfield, Waynesville and Fort Leonard Wood. The use of such facilities has the effect of causing propane prices to rise.⁹¹

85. The effect of the introduction of natural gas into a propane market is to substantially reduce the demand for propane. This necessarily raises costs for those propane customers that do not, or cannot, convert to natural gas.⁹²

86. The grant of the certificate to Southern Missouri Gas could severely affect the business of some propane dealers in the area.⁹³

87. Ed Simmons, a propane dealer and member of the MPGA, testified that it would never be in the economic interest of propane dealers to permit a natural gas company to enter an area with a propane market.⁹⁴

88. Southern Missouri Gas currently has an ACA balance between \$220,453 and \$378,470 that Staff has recommended be disallowed.⁹⁵ Southern Missouri Gas has represented to the Commission that a disallowance of this scale would be detrimental to

⁸⁹ Tr. p. 179.

⁹⁰ Tr. p. 206.

⁹¹ Tr. pp. 210-212.

⁹² Tr. pp. 210-212.

⁹³ Tr. p. 214, lines 16-25.

⁹⁴ Tr. p. 231.

⁹⁵ Ex. 11.

the Company's ability to continue to provide safe and adequate service throughout its Missouri service areas.⁹⁶

89. Southern Star is a wholesale gas transportation service supplier of Southern Missouri Gas.⁹⁷

90. Southern Missouri Gas proposes to provide natural gas distribution through a city gate delivery point from an interconnection point with the Southern Star pipeline (Station 142 near Rogersville).⁹⁸

91. Station 142 is the end of the Southern Star pipeline and the beginning of the Southern Missouri Gas system.⁹⁹

92. Southern Missouri Gas has already contracted for the necessary gas to serve Lebanon, Houston and Licking, plus a reserve margin of 20%.¹⁰⁰

93. Southern Missouri Gas has not experienced any pressure problems on its portion of the Southern Star pipeline.¹⁰¹

94. Exhibit 9 shows that the monthly pressure tests at Station 142 have shown constant results.¹⁰²

⁹⁶ Ex. 11; and Tr. p. 86.

⁹⁷ Tr. p. 63, line 12, to p. 64, line 4.

⁹⁸ Tr. p. 63, line 20,

⁹⁹ Tr. p. 161, lines 15-16.

¹⁰⁰ Tr. pp. 63-64.

¹⁰¹ Ex. 9; Tr. pp. 68-69.

¹⁰² Ex. 9; Tr. pp. 68-69.

95. Mr. Simmons' testimony regarding pressure problems was not based on any personal knowledge and was based on other areas of the system not related to the current applications.¹⁰³

96. Southern Missouri Gas pledges to operate in accordance with the current safety rules of the Commission.¹⁰⁴

97. If the certificates are granted promptly, Southern Missouri Gas estimates that service will be available in Lebanon by December 2007 or January 2008.¹⁰⁵

98. Southern Missouri Gas expects to spend about \$11 million to build transmission lines to Lebanon, Houston and Licking, and another \$1.7 million to build distribution lines in those communities.¹⁰⁶

99. Southern Missouri Gas anticipates adding approximately twelve additional employees to provide service to the communities of Lebanon, Houston, and Licking.¹⁰⁷

100. Southern Missouri Gas and the customers to be served would share the cost of providing service to a particular area or customer according to the provisions of Southern Missouri Gas's tariffs which are similar to other local distributor companies in Missouri.¹⁰⁸

101. Southern Missouri Gas would bear the total cost of laying a 2-inch distribution main along a street.¹⁰⁹

¹⁰³ Tr. p. 209, and pp. 233-234.

¹⁰⁴ Tr. p. 64, lines 15-18.

¹⁰⁵ Tr. p. 112, lines 4-18.

¹⁰⁶ Tr. p. 120, lines 12-14, and p. 121, lines 24-25.

¹⁰⁷ Tr. p. 64, lines 13-14.

¹⁰⁸ Tr. pp. 305-307.

¹⁰⁹ Tr. p. 125, lines 7-12.

102. The cost of the service lines and meters would be shared by Southern Missouri Gas and the customer. Each meter costs \$300 to \$400.¹¹⁰

103. Southern Missouri Gas estimates that conversion from propane or electricity to natural gas will cost about \$1,500 per residential customer, including the cost of the main.

104. The gas service tariff of Southern Missouri Gas allows it to pay \$250 of the conversion cost per residential customer.

105. Southern Missouri Gas has a website which states, “If you want to convert your home from propane or electricity to natural gas, SMNG will run a gas line to your house, set a meter, and convert up to three (3) appliances at no charge to you.”¹¹¹

106. In October 2005, Public Counsel filed a complaint before the Commission alleging that Southern Missouri Gas was not following Commission rules regarding hedging practices. That case was resolved by a stipulation and agreement.¹¹²

107. The applications for certificates to serve Lebanon, Houston, and Licking filed by Southern Missouri Gas include all the information necessary for a Commission determination.

Conclusions of Law

The Missouri Public Service Commission has arrived at the following conclusions of law.

¹¹⁰ Tr. p. 125, lines 13-23.

¹¹¹ Ex. 14.

¹¹² Tr. pp. 145-146.

Southern Missouri Gas is a “gas corporation” and a “public utility” under the jurisdiction of the Commission under Chapters 386 and 393, RSMo.¹¹³

The Commission has authority under Section 393.170, RSMo, to grant permission and approval for the “construction of a gas plant.” Section 392.170 states in part:

2. . . . Before such certificate shall be issued a certified copy of the charter of such corporation shall be filed in the office of the commission, together with a verified statement of the president and secretary of the corporation, showing that it has received the required consent of the proper municipal authorities.

3. The commission shall have the power to grant permission and approval herein specified whenever it shall after due hearing determine that such construction or such exercise of the right, privilege or franchise is necessary or convenient for the public service. The commission may by its order impose such condition or conditions as it may deem reasonable and necessary. Unless exercised within a period of two years from the grant thereof, authority conferred by such certificate of convenience and necessity issued by the commission shall be null and void.

Section 393.170.3, set out above, authorizes this Commission to grant a certificate of convenience and necessity when it determines, after due hearing, that the proposed project is “necessary or convenient for the public service.” It has been held that the term “necessity” does not mean “essential” or “absolutely indispensable,” but rather that the proposed project “would be an improvement justifying its cost,”¹¹⁴ and that the

¹¹³ All statutory references are to the Revised Statutes of Missouri 2000 as supplemented by the Cumulative Supplement of 2006 unless otherwise noted.

¹¹⁴ *St. ex rel. Intercon Gas, Inc. v. Public Service Commission*, 848 S.W.2d 593, 597 (Mo. App., W.D. 1993); *St. ex rel. Beaufort Transfer Co. v. Clark*, 504 S.W.2d 216, 219 (Mo. App. 1973).

inconvenience to the public occasioned by lack of the proposed service is great enough to amount to a necessity.¹¹⁵

It is within the Commission's discretion to determine when the evidence indicates the public interest would be served by the award of the certificate.¹¹⁶ However, the Commission may not grant a certificate of convenience and necessity unless the applicant has already obtained a local franchise, which is an "absolute prerequisite."¹¹⁷

The MPGA suggests that the standard the Commission must follow is set out by its previous cases. The standard governing this matter is actually set by statute as noted above. The Commission may grant a certificate of convenience and necessity if it determines, after hearing, that it is "necessary or convenient for the public service."¹¹⁸ The Commission has, however, previously set out criteria which it has used to evaluate natural gas certificate applications. Those criteria are: (1) a need for the service; (2) the applicant is qualified to provide the proposed service; (3) the applicant has the financial ability to provide the service; (4) the applicant's proposal is economically feasible; and (5) the service promotes the public interest.¹¹⁹

If the Commission grants the requested certificates to Southern Missouri Gas, the company will have an obligation to serve the public in its allotted service areas.¹²⁰ *Harline*

¹¹⁵ *Beaufort Transfer Co., supra; St. ex rel. Transport Delivery Service v. Burton*, 317 S.W.2d 661 (Mo. App. 1958).

¹¹⁶ *Intercon Gas, supra, quoting St. ex rel. Ozark Electric Coop. v. Public Service Commission*, 527 S.W.2d 390, 392 (Mo. App. 1975).

¹¹⁷ *St. ex inf. Shartel ex rel. City of Sikeston v. Missouri Utilities Co.*, 331 Mo. 337, 350, 53 S.W.2d 394, 399 (Mo. banc 1932).

¹¹⁸ Section 393.170.3, RSMo.

¹¹⁹ *Re Intercon Gas, Inc.*, 30 Mo P.S.C. (N.S.) 554, 561 (1991).

¹²⁰ *State ex rel. Harline v. Public Service Commission*, 343 S.W.2d 177, 181 (Mo. App. 1960).

provides as follows regarding a public utility's obligation to serve in its certificated service territory:

The certificate of convenience and necessity is a mandate to serve the area covered by it, because it is the utility's duty, within reasonable limitations, to serve all persons in an area it has undertaken to serve.¹²¹

If Houston or Licking exercise their options to purchase the local distribution system within the municipality, it may place Southern Missouri Gas in violation of the order in Commission Case No. GA-94-127, in which the Commission stated “that Tartan [the predecessor of Southern Missouri Gas and of Southern Missouri Natural Gas] provide only retail natural gas service to the ten municipalities from which it has received franchises . . .” [Commission Report and Order, Case No. GA-94-127, p. 9].¹²² Thus, to remain in compliance with Commission orders, it would be necessary for the company to seek a waiver from that provision.

Southern Missouri Gas and its customers share the cost of providing service to a particular area or specific customer according to the provisions of the tariffs of Southern Missouri Gas.¹²³ Those tariffs are similar to the tariffs of other local distributor companies in Missouri.¹²⁴

Commission Rule 4 CSR 240-3.205 requires a gas company applying for a certificate of convenience and necessity to include in its application, a “plat drawn to scale

¹²¹ *State ex rel. Ozark Power & Water Co. v. Public Service Commission*, 287 Mo. 522, 229 S.W. 782; *State ex rel. Kansas City Power & Light Co. v. Public Service Commission of Missouri et al.*, 335 Mo. 1248, 76 S.W.2d 343; *State ex rel. Federal Reserve Bank of Kansas City v. Public Service Commission*, 239 So. 531, 191 S.W.2d 307; and *May Department Stores Co. v. Union Electric Light & Power Co.*, 341 Mo. 299, 107 S.W.2d 41.

¹²² Tr. p. 248, lines 15-21.

¹²³ Tr. pp. 305-307.

¹²⁴ Tr. pp. 305-307.

of one-half inch (1/2") to the mile on maps comparable to county highway maps issued by the Missouri Department of Transportation or a plat drawn to a scale of two thousand feet (2,000') to the inch." Even though the maps included with the application were not similar to the county maps referenced in the rule, they were sufficient to determine the proposed service area which is the purpose for the rule. In addition, given that the metes and bounds descriptions are included, there can be no mistake as to the service area. Finally, no harm or prejudice was alleged to have come to any of the parties because of the quality of the maps submitted, and therefore, the Commission concludes that the maps attached to the application are in compliance with the Commission's rule.

Decision

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. After applying the facts as it has found them to its conclusions of law, the Commission has reached the following decision.

The evidence adduced shows that the proposed expansion of the natural gas service territory of Southern Missouri Gas into Lebanon, Houston and Licking is economically feasible, will meet a definite need in those communities, and will confer tangible economic benefits upon them.

There is a need for the service. This need is evidenced by the fact that the cities have consistently each granted Southern Missouri Gas a franchise, and with regard to Lebanon, a vast majority of the voters have approved that franchise. The communities are

in the best position to assess whether there is a need or desire for natural gas service, and from the actions of those communities it is obvious that such a need exists. In addition, Joe Knapp, the City Administrator for the City of Lebanon, testified that the City of Lebanon had been losing economic development opportunities because of the lack of natural gas service in the area. Mr. Knapp also testified that current industries have been requesting natural gas service.

Southern Missouri Gas also showed that the grant of the certificates would bring benefits in the form of choice of an economical method of energy. In addition, the added volume to the system as a whole could benefit all the customers on the system.

One of the possible detriments of granting the certificate is the risk of failure being placed on the current ratepayers in the system. The evidence also shows that the expansion may severely affect the business of propane dealers in those communities and may have an adverse effect on propane prices in those communities. On balance, however, the benefits that the expansion will confer will outweigh those detriments. The Commission therefore concludes that the grant of the proposed certificates of convenience and necessity is necessary and convenient for the public interest.

The Commission further determines that if acceptable financing can be obtained without excessive risk to the current ratepayers, the grant of certificates is in the public interest. Thus, the Commission determines it is reasonable and necessary to place certain conditions on the grant of the requested certificate. As proposed by Staff and Public Counsel, the certificates of convenience and necessity will be conditioned on Southern Missouri Gas obtaining financing which is approved by the Commission, and on the shareholders, rather than the ratepayers, being deemed responsible for the detrimental

effects of a loss resulting from inaccurate estimations of customer conversion or usage rates. Finally, Southern Missouri Gas is notified that if a city elects to purchase the system, a waiver from the previous Commission order may be required.

IT IS ORDERED THAT:

1. The applications for a certificate of convenience and necessity filed by Southern Missouri Gas Company, L.P., d/b/a Southern Missouri Natural Gas, on December 6, 2006, and February 7, 2007, are hereby granted with the conditions set out below.

2. Southern Missouri Gas Company, L.P., d/b/a Southern Missouri Natural Gas, is granted a certificate of public convenience and necessity to expand its backbone pipeline system and to construct, install, own, operate, control, manage, a gas distribution system for the public, as proposed in its applications, in the Cities of Lebanon, Licking, and Houston, Missouri, as an expansion of its presently certificated area, as conditioned herein.

3. The certificates granted in Ordered Paragraphs No. 1 and 2, above, are conditioned upon the Company's obtaining financing acceptable to the Commission.

4. The certificates granted in Ordered Paragraphs No. 1 and 2, above, are conditioned upon the shareholders assuming responsibility for any loss associated with inaccurate estimations of the customer conversion rate or of customer usage rates.

5. The Commission makes no finding as to the prudence or ratemaking treatment to be given any costs or expenses incurred as the result of the granting of this certificate of convenience and necessity, and reserves the right to make any disposition of costs and expenses which it deems reasonable, in any future ratemaking proceeding.

6. This Report and Order shall become effective on August 26, 2007.

BY THE COMMISSION

A handwritten signature in black ink, appearing to read 'Colleen M. Dale', written over a horizontal line.

Colleen M. Dale
Secretary

(S E A L)

Davis, Chm., Murray, Gaw, and
Appling, CC., concur;
Clayton, C., dissents; a separate
dissenting opinion may follow;
and certify compliance with
Section 536.080, RSMo 2000.

Dated at Jefferson City, Missouri,
on this 16th day of August, 2007.