STATE OF MISSOURI
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held at its office in Jefferson City on the 22nd day of December, 2005.

Office of the Public Counsel,	)	
	)	
Complainant,	)	
	)	
v.	)	**Case No. GC-2006-0180**
	)	
Southern Missouri Gas Company, L.P.,	)	
	)	
Respondent.	)	

ORDER DENYING MOTION TO DISMISS

Issue Date: December 22, 2005 Effective Date: December 22, 2005

Procedural History:

On October 21, 2005, the Public Counsel filed his Complaint against Southern Missouri Gas Company, L.P. ("SMG"), alleging that the Company has failed to comply with Commission Rule 4 CSR 240-40.018, which requires Missouri's Local Distribution Companies to "undertake diversified natural gas purchasing activities as part of a prudent effort to mitigate downward natural gas price volatility and secure adequate natural gas supplies for their customers," but instead "established a strategy that was entirely a gamble based on a hope that market prices would decline this fall and winter." The Public Counsel prays that the Commission will find SMG to be in continuing violation of its rule and will impose "appropriate penalties" on SMG for its non-compliance.

The Commission issued its Notice of Complaint on October 24 and SMG timely filed its Answer and Motion to Dismiss on November 23. Public Counsel has not made any response to SMG's Motion to Dismiss nor replied to its affirmative defenses and the interval for doing so has now passed.

Discussion:

SMG's Motion to Dismiss

SMG states numerous grounds for dismissal. They are summarized below:

1. The Complaint is fatally defective because it does not contain the information required by Commission Rule 4 CSR 240-2.070(5).

2. The Complaint fails to state a claim upon which relief may be granted because Public Counsel does not allege that he is "aggrieved" as required by Commission Rule 4 CSR 240-2.070 or that SMG has caused harm to anyone.

3. The Complaint fails to state a claim upon which relief can be granted.

4. Commission Rule 4 CSR 240-40.018 is "ambiguous and vague" and thus cannot be the basis of a penalty action.

5. Commission Rule 4 CSR 240-40.018 does not specify what conduct is required and thus cannot be the basis of a penalty action.

6. Commission Rule 4 CSR 240-40.018 is advisory only and thus cannot be the basis of a penalty action.

7. Commission Rule 4 CSR 240-40.018 does not require any particular actions within any specified time period and thus cannot be the basis of a penalty action.

8. Commission Rule 4 CSR 240-40.018 does not include any penalties and thus cannot be the basis of a penalty action.

9. The Commission may not impose penalties for the violation of Commission Rule 4 CSR 240-40.018 because the Commission would thereby "interfere with interstate commerce."

10. The Commission lacks authority to impose penalties on SMG for engaging in lawful, unregulated activities.

11. The Commission lacks authority "to mandate the specific pricing structures, mechanisms and instruments that must be used by [SMG] in rendering service to its customers" because "[s]uch actions by the Commission would constitute an unlawful invasion of the management functions of the public utility."

Rule 4 CSR 240-40.018

Public Counsel charges that SMG has violated Commission Rule 4 CSR 240-40.018, which provides:

> (1) Natural Gas Supply Planning Efforts to Ensure Price Stability.
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> (A) As part of a prudent planning effort to secure adequate natural gas supplies for their customers, natural gas utilities should structure their portfolios of contracts with various supply and pricing provisions in an effort to mitigate upward natural gas price spikes, and provide a level of stability of delivered natural gas prices.
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> (B) In making this planning effort, natural gas utilities should consider the use of a broad array of pricing structures, mechanisms, and instruments, including, but not limited to, those items described in (2)(A) through (2)(H), to balance market price risks, benefits, and price stability. Each of these mechanisms may be desirable in certain circumstances, but each has unique risks and costs that require evaluation by the natural gas utility in each circumstance. Financial gains or losses associated with price volatility mitigation efforts are flowed through the Purchased Gas Adjustment (PGA) mechanism, subject to the applicable provisions of the natural gas utility's tariff and applicable prudence review procedures.

(C) Part of a natural gas utility's balanced portfolio may be higher than spot market price at times, and this is recognized as a possible result of prudent efforts to dampen upward volatility.

(2) Pricing Structures, Mechanisms and Instruments:

(A) Natural Gas Storage;

(B) Fixed Price Contracts;

(C) Call Options;

(D) Collars;

(E) Outsourcing/Agency Agreements;

(F) Futures Contracts; and

(G) Financial Swaps and Options from Over the Counter Markets; and

(H) Other tools utilized in the market for cost-effective management of price and/or usage volatility.

Threshold Matters

SMG first argues for dismissal on the grounds that the cited rule cannot be violated because it is "advisory only." SMG also contends that no penalty will lie because the rule does not expressly provide for a penalty.

SMG's failure to support its Motion to Dismiss with suggestions leaves the Commission uncertain as to the meaning of its contention that the Complaint must be dismissed because Rule 4 CSR 240-40.018 is "advisory only." Something is "advisory" when it is not binding.[1] SMG evidently asserts that the rule, which states that "natural gas utilities *should* structure their portfolios of contracts . . . in an effort to mitigate upward

[1] *See, e.g., Blackburn v. Mackey,* 131 S.W.3d 392, 399 (Mo. App., W.D. 2004): "The court in a dissolution or modification case is not bound by the terms of an agreement between the parties with regard to custody, support, or visitation of children. Stipulations regarding child support are advisory only; the court alone bears the ultimate responsibility of ensuring that a child support decree reflects the best interests of the child." (Internal citations omitted.)

natural gas price spikes, and provide a level of stability of delivered natural gas prices," is merely hortatory. SMG goes on to state, "[the rule] does not require any mandatory or specific actions by the public utility[.]" The Commission disagrees.

The rule must be viewed in the context within which SMG actually operates. SMG is a "local distribution company" or "LDC" and is in the business of selling natural gas at retail to the public. This is an activity subject to regulation by this Commission. Like all LDCs, SMG has Purchased Gas Adjustment (PGA) and Actual Cost Adjustment (ACA) clauses in its approved tariffs that permit it to adjust its rates on the basis of forecasts of wholesale natural gas prices, subject to an annual audit and true-up.[2] Part of the annual audit and true-up process is the disallowance of imprudent costs incurred in acquiring natural gas at wholesale. When viewed in this context, the language of Rule 4 CSR 240-40.018 is hardly hortatory. SMG's natural gas purchasing practices are, in fact, subject to an annual prudence review.

An additional consideration highlights the importance of compliance with Rule 4 CSR 240-40.018. Natural gas is used by many consumers to heat their homes in the winter. An LDC's failure to comply with Rule 4 CSR 240-40.018 may well result in rates that consumers cannot easily pay. The after-the-fact annual true-up under the ACA process provides little comfort to families that cannot afford to heat their homes in the winter or, if able to pay the heating bills, nonetheless suffer from having to tighten their

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[2] *See St. ex rel. Midwest Gas Users' Association v. Public Service Commission of the State of Missouri,* 976 S.W.2d 470, 474 (Mo. App., W.D. 1998): "a PGA clause allows a local distribution company to automatically adjust the rates it charges its customers in proportion to the change in the rate the local distribution company is charged by its wholesale suppliers. At the end of every twelve-month period, the local distribution company then makes an actual cost adjustment ("ACA") filing with the PSC so that the PSC can determine whether the estimated amount previously charged customers accurately reflects the actual cost to the utility of the gas supplied."

belts unduly in other areas of the family budget. For these reasons, the Commission concludes that Rule 4 CSR 240-40.018 is not merely advisory, but rather imposes an obligation on LDCs that they are expected to meet.

It is also unavailing to SMG that Rule 4 CSR 240-40.018 does not specify any penalty for its violation. The penalty has been provided by the legislature at Section 386.570, RSMo.

Validity of the Rule

SMG next asserts that the Complaint must be dismissed because the Commission is without authority to seek penalties with respect to its "unregulated activities permitted by law" or to "mandate the specific pricing structures, mechanisms and instruments that must be used by [SMG] in rendering service to its customers."

To the extent that SMG challenges the validity of Rule 4 CSR 240-40.018, these contentions are beyond the Commission's authority to adjudicate. Administrative rules, duly promulgated pursuant to properly-delegated statutory authority, have "the force and effect of law, unless and until they are invalidated by judicial decision[.]"[3] The Public Service Commission's "adjudicative power extends only to the ascertainment of facts and the application of existing law thereto in order to resolve issues within the given area of agency expertise."[4] The Commission cannot determine the validity of an administrative rule because that "is purely a judicial function."[5]

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[3] *State ex rel. Danforth v. Riley,* 499 S.W.2d 40, 44 (Mo. App., W.D. 1973).

[4] *State Tax Commission v. Administrative Hearing Commission,* 641 S.W.2d 69, 75 (Mo. banc 1982).

[5] *Id.*

In any event, the cited rule applies to SMG's activity of purchasing natural gas at wholesale for retail sale to the public. This activity is not unregulated, as already discussed. SMG faces an annual prudence review and true-up by this Commission and costs incurred in imprudent purchases of natural gas will be disallowed. Neither does the Commission agree that the rule impermissibly invades the functions of SMG's management.[6] The rule does not, contrary to SMG's claim, "mandate the specific pricing structures, mechanisms and instruments that must be used by [SMG] in rendering service to its customers," rather, it simply directs the Company to use some strategy of price-spike mitigation. Additionally, the right of a utility's board to manage the company free of undue Commission interference is not absolute. As the Missouri Supreme Court has said, "The company has a lawful right to manage its own affairs and conduct its business in any way it may choose, *provided that in so doing it does not injuriously affect the public."*[7] Rule 4 CSR 240-40.018 is intended to prevent the LDC's management from injuriously affecting the public.

Constitutional Issues

SMG also contends that the United States Constitution requires dismissal, first, because Rule 4 CSR 240-40.018 violates the due process clause because it is impermissibly vague and, second, because it constitutes an impermissible burden on interstate commerce in violation of the so-called "dormant" commerce clause.

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[6] It is well-established that the Commission lacks authority to take over the management of regulated entities. *St. ex rel. Southwestern Bell Telephone Co. v. Missouri Public Service Commission,* 262 U.S. 276, 43 S.Ct. 544, 67 L.Ed. 981 (1923); *St. ex rel. City of St. Joseph v. Public Service Commission,* 325 Mo. 209, 30 S.W.2d 8 (banc 1930); *St. ex rel. Laclede Gas Co. v. Public Service Com.,* 600 S.W.2d 222, 227-228 (Mo. App., W.D. 1980); *St. ex rel. Harline v. Public Service Commission,* 343 S.W.2d 177 (Mo. App. 1960).

[7] *St. ex rel. St. Joseph v. Public Service Com.,* 325 Mo. 209, 223, 30 S.W.2d 8, 14 (Mo. 1930) (emphasis added).

The Missouri Supreme Court has stated that it is a basic principle of due process that an enactment is void for vagueness if it does not clearly define the conduct that is required or prohibited.[8] The void for vagueness doctrine ensures that laws give fair and adequate notice of proscribed conduct and protect against arbitrary and discriminatory enforcement.[9] The test for vagueness is whether the language conveys to a person of ordinary intelligence a sufficiently definite warning as to the proscribed – or required -- conduct when measured by common understanding and practices.[10] However, "neither absolute certainty nor impossible standards of specificity are required in determining whether terms are impermissibly vague."[11]

Rule 4 CSR 240-40.018 states that "natural gas utilities should structure their portfolios of contracts with various supply and pricing provisions in an effort to mitigate upward natural gas price spikes, and provide a level of stability of delivered natural gas prices." These words are not unconstitutionally vague. Rather, the Commission determines that they meet the constitutional standard because they "provide fair notice of the required conduct."[12] The Commission concludes that the Complaint need not be dismissed because Rule 4 CSR 240-40.018 is not void for vagueness.

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[8] *State v. Brown,* 140 S.W.3d 51, 54 (Mo. banc 2004); *Cocktail Fortune, Inc. v. Supervisor of Liquor Control,* 994 S.W.2d 955, 957 (Mo. banc 1999). The due process clause is found in the XIVth Amendment to the United States Constitution.

[9] *Brown, supra,* 140 S.W.3d at 54; *State v. Entertainment Ventures I, Inc.,* 44 S.W.3d 383, 386 (Mo. banc 2001).

[10] *State ex rel. Zobel v. Burrell,* 167 S.W.3d 688, 692 (Mo. banc 2005); *Brown, supra,* 140 S.W.3d at 54; *Cocktail Fortune, Inc., supra,* 994 S.W.2d at 957.

[11] *Zobel, supra,* 167 S.W.3d at 692; *Brown, supra,* 140 S.W.3d at 54.

[12] *Brown, supra,* 140 S.W.3d at 54.

SMG also contends that the complaint must be dismissed because the enforcement of Rule 4 CSR 240-40.018 would "interfere with interstate commerce." SMG presumably refers to the so-called "dormant" commerce clause, which prohibits states from discriminating against out-of-state businesses.[13] The Supreme Court has explained it:

> Our Constitution was framed upon the theory that the peoples of the several States must sink or swim together. Thus, this Court has consistently held that the Constitution's express grant to Congress of the power to regulate Commerce among the several States, contains a further, negative command, known as the dormant Commerce Clause, that creates an area of trade free from interference by the States. This negative command prevents a State from jeopardizing the welfare of the Nation as a whole by placing burdens on the flow of commerce across its borders that commerce wholly within those borders would not bear.[14]

SMG has not explained how the collection of penalties for violating Rule 4 CSR 240-40.018 would violate the dormant commerce clause. Neither Rule 4 CSR 240-40.018 nor Section 386.570, RSMo, facially discriminates against out-of-state entities. Indeed, the Missouri Public Service Commission Act does not apply to interstate commerce "except insofar as the same may be permitted under the provisions of the Constitution of the United States and the acts of Congress."[15] SMG is a Missouri-regulated utility and Public Counsel seeks penalties for conduct that occurred within Missouri. As the United States Supreme Court has said:

> Although we have long since rejected any suggestion that a state tax affecting interstate commerce is immune from Commerce Clause scrutiny because it attaches only to a 'local' or intrastate activity, we have also made clear that the Constitution neither displaces States'

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[13] U.S. Constitution, Art. I, § 8, cl. 3.

[14] *American Trucking Associations, Inc., and USF Holland, Inc. v. Michigan Public Service Commission,* ___ U.S. ___, ___, 125 S. Ct. 2419, 2422-2423, 162 L. Ed. 2d 407, 412 (2005) (internal quotation marks and citations omitted).

[15] Section 386.030, RSMo.

> authority to shelter their people from menaces to their health or safety, nor unduly curtails States' power to lay taxes for the support of state government.[16]

The Commission concludes that the dormant commerce clause does not require that the Complaint herein be dismissed.

Technical Pleading Defects

SMG next argues that the Complaint must be dismissed because it fails to comply with Commission Rule 4 CSR 240-2.070:

> As fully set forth in Subsections (1) [sic] of the Commission's Rule 4 CSR 240-2.070, the complainant must be aggrieved by a violation of any statute, rule, order or decision within the Commission's jurisdiction. While the Complaint alleges that SMGC violated the terms of Rule 4 CSR 240-40.018, the Complainant fails to allege that it is aggrieved by a violation of the rule, or that the alleged actions taken by SMGC related to its gas purchasing practices in any way resulted in harm to the Complainant or SMGC's ratepayers.

As an additional ground for dismissal, SMG states:

> The instant Complaint fails to comply with the requirements set forth in Commission Rule 4 CSR 240-2.070, in that it does not contain the information required in Subsection (5) of said Rule. Among the deficiencies, most notable is the omission of any statement regarding "[t]he jurisdiction of the commission over the subject matter of the complaint". In addition, the Complaint fails to include a "statement as to whether the complainant has directly contacted the person, corporation or public utility about which complaint is being made."
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> Subsections (1) and (5) of Commission Rule 4 CSR 240-2.070 state as follows:
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> (1) The commission on its own motion, the commission staff through the general counsel, the office of the public counsel, or any person or public utility who feels aggrieved by a violation of any statute, rule, order or decision within the commission's jurisdiction may file a complaint. The aggrieved party, or complainant, has the option to file either an informal or a formal complaint.
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> * * *

[16] *American Trucking Associations, supra* (internal quotation marks and citations omitted).

(5) The formal complaint shall contain the following information:

(A) The name, street address, signature**,** telephone number, facsimile number and electronic mail address, where applicable, of each complainant and, if different, the address where the subject utility service was rendered;

(B) The name and address of the person, corporation or public utility against whom the complaint is being filed;

(C) The nature of the complaint and the complainant's interest in the complaint, in a clear and concise manner;

(D) The relief requested;

(E) A statement as to whether the complainant has directly contacted the person, corporation or public utility about which complaint is being made;

(F) The jurisdiction of the commission over the subject matter of the complaint; and

(G) If the complainant is an association, a list of all its members.

Rule 4 CSR 240-2.070(1) authorizes the "Office of the Public Counsel" to file a complaint. Under the rule of the last antecedent, the modifying phrase "who feels aggrieved by a violation of any statute, rule, order or decision within the commission's jurisdiction" does not apply to the Office of the Public Counsel, but only to the immediately preceding phrase, "any person or public utility."[17] The rule tracks the language of Section 386.390.1, RSMo, which authorizes the Commission to hear and determine complaints.

Section 386.390.1, RSMo, authorizes the Commission to determine complaints as to "any act or thing done or omitted to be done by any corporation, person or public

[17] "The last antecedent rule generally requires that relative and qualifying words, phrases or clauses must be applied to the words, phrases or clauses immediately preceding and are not to be construed as extending to or including others more remote." *Blue Cross & Blue Shield of Kan. City, Inc. v. Nixon,* 26 S.W.3d 218, 233-234 (Mo. App., W.D. 2000).

utility . . . in violation, or claimed to be in violation, of any provision of law, or of any rule or order or decision of the commission[.]" The Public Counsel is expressly authorized to bring such a complaint and thus need not plead that he is aggrieved. A complaint brought under this authority necessarily must include an allegation of a violation of a law or of a Commission rule, order or decision;[18] however, it need not contain an allegation of injury to anyone. The Commission concludes that Public Counsel's Complaint meets the pleading requirements of Rule 4 CSR 240-2.070(1).

As for SMG's assertion that the Complaint must be dismissed because the Public Counsel failed to comply with the pleading requirements in subsection (5) of Rule 4 CSR 240-2.070, the Commission concludes that it is without merit.

Failure to State a Claim

SMG also argues that the Complaint must be dismissed because it fails to state a claim upon which relief may be granted. The consideration of such motions was, at one time, limited to matters contained within the four corners of the complaint; however, the modern trend is to extend consideration to matters outside the complaint as well.[19] All well-pleaded factual allegations in the complaint must be accepted as true and the facts must be liberally construed to support the complaint.[20] Complainant enjoys the benefit of all reasonable inferences.[21] The complaint should not be dismissed unless it shows no set

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[18] *St. ex rel. Ozark Border Electric Cooperative v. PSC,* 924 S.W.2d 597, 599-600 (Mo. App., W.D. 1996).

[19] Devine, *Missouri Civil Pleading & Practice,* pg. 264 and Section 24-2 (1986).

[20] *Nazeri v. Missouri Valley College,* 860 S.W.2d 303, 306 (Mo. banc 1993).

[21] *Id.*

of facts entitling it to relief.[22] Additionally, a complaint under the Public Service Commission Law is to be judged against the standard of notice pleading rather than the stricter standard of fact pleading.[23] However, where a statute or a controlling judicial decision imposes a specific pleading requirement on an administrative complaint, strict compliance is required.[24]

The gravamen of Public Counsel's complaint is his accusation that SMG has violated Rule 4 CSR 240-40.018, which provides at (1)(A):

> As part of a prudent planning effort to secure adequate natural gas supplies for their customers, natural gas utilities should structure their portfolios of contracts with various supply and pricing provisions in an effort to mitigate upward natural gas price spikes, and provide a level of stability of delivered natural gas prices.

Public Counsel accuses SMG of failing to conduct itself as the rule requires, stating:

> Despite the negative impacts this increase will impose upon its customers, SMG has failed and/or refused to implement any of the pricing structures, mechanisms or instruments set forth by the Commission in the above Rule. The only thing SMG has done is to lock in a discount off of the market price which does absolutely nothing to protect its customers from the volatility of the market price. In fact, rather than establish a purchasing strategy that would "mitigate upward natural gas price spikes, and provide a level of stability of delivered natural gas prices," SMG established a strategy that was entirely a gamble based on a hope that market prices would decline this fall and winter.

Contrary to SMG's assertion, the Commission concludes that Public Counsel's Complaint does indeed state a claim in that it alleges that SMG has violated Rule 4 CSR

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[22] *Id.*

[23] *Sorbello v. City of Maplewood,* 610 S.W.2d 375, 376 (Mo. App., E.D. 1980); *Schrewe v. Sanders,* 498 S.W.2d 775, 777 (Mo. 1973); *and see St. ex rel. Kansas City Terminal Railway Co. v. Public Service Commission,* 308 Mo. 359, 372, 272 S.W. 957, 960 (banc 1925).

[24] *Abrams v. Ohio Pacific Exp.,* 819 S.W.2d 338, 342 (Mo. banc 1991) (time limitations); *Farmer v. Barlow Truck Lines, Inc.,* 1998 WL 418740, *4 (Mo. App., W.D. 1998) (procedure for review of awards).

240-40.018 by failing to engage in a prudent natural gas procurement planning effort in order to mitigate upward price spikes. In the event that Public Counsel proves his case, Section 386.570, RSMo, provides for a penalty.

IT IS THEREFORE ORDERED:

1. That the Motion to Dismiss filed by Southern Missouri Gas Company, L.P., with its Answer on November 23, 2005, is denied.

2. That this order shall become effective on December 22, 2005.

BY THE COMMISSION

Colleen M. Dale
Secretary

(S E A L)

Davis, Chm., Gaw, Clayton, and
Appling, CC., concur.
Murray, C., dissents, with separate
dissenting opinion attached.

Thompson, Deputy Chief Regulatory Law Judge