

# BEFORE THE PUBLIC SERVICE COMMISSION

## OF THE STATE OF MISSOURI

In the matter of the application of Missouri Gas )  
Company for permission, approval, and a certificate of )  
public convenience and necessity authorizing it to )  
construct, install, own, operate, control, manage and )  
maintain a natural gas transmission pipeline and related ) Case No. GA-95-231  
facilities and to transport natural gas in portions of )  
Phelps and Dent Counties, Missouri, from the City of )  
Rolla, Missouri, to a point at or near the City of )  
Salem, Missouri. )  
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### REPORT AND ORDER

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**Issue Date:** August 8, 1995

**Effective Date:** August 18, 1995

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Rolla, Missouri, to a point at or near the City of )  
Salem, Missouri. )  
)

**APPEARANCES**

**James C. Swearengen**, Brydon, Swearengen & England, P.C., 312 East Capitol Avenue,  
Post Office Box 456, Jefferson City, Missouri, 65102, for Missouri Gas Company.

**Lewis R. Mills, Jr.**, Deputy Public Counsel, Office of Public Counsel, Post Office  
Box 7800, Jefferson City, Missouri 65102, for the Office of Public Counsel and  
the public.

**Aisha Ginwalla**, Assistant General Counsel, Missouri Public Service Commission,  
Post Office Box 360, Jefferson City, Missouri 65102, for the staff of the  
Missouri Public Service Commission.

**ADMINISTRATIVE**

**LAW JUDGE:** Thomas H. Luckenbill, Deputy Chief.

**REPORT AND ORDER**

**Procedural History**

On February 10, 1995, Missouri Gas Company (MoGas or Company) filed  
an application with the Commission for a certificate of convenience and necessity  
authorizing it to construct, own, operate, control, manage and maintain a natural  
gas transmission pipeline and related facilities and to transport natural gas in  
portions of Phelps and Dent Counties, Missouri, from a point near the City of  
Rolla, Missouri, to a point near the City of Salem, Missouri (proposed Salem  
delivery spur).

A map and description of the general route and location of the proposed Salem delivery spur is attached to the application and marked as Schedule 2. A document which sets out the plans and specifications for the proposed Salem delivery spur is attached to the application and marked as Schedule 4. A list of electric and telephone lines of regulated and nonregulated utilities, railroad tracks and underground facilities which the proposed Salem delivery spur will cross was filed on March 28, 1995 and marked as Schedule 5.

On February 24, 1995, the Commission issued an Order And Notice which provided notice of the application and an opportunity to request intervention in the proceeding. No person requested intervention.

On February 23, 1995, the Commission's Staff filed a motion to consolidate this case with Case GA-95-216, which is the application of Missouri Public Service, a division of UtiliCorp United Inc., for a certificate of convenience and necessity to distribute natural gas in Salem, Missouri. On March 1, 1995, the Commission issued an order denying Staff's motion to consolidate the cases.

On March 28, 1995, the Commission issued an Order Setting Procedural Schedule. The Company had already filed its direct testimony on March 10, 1995. Staff witnesses Flowers, Hubbs, Winter and Moore filed rebuttal testimony on May 19, 1995. Company witnesses Kreul and Miller filed surrebuttal testimony on June 2, 1995.

On June 16, 1995, the parties filed a hearing memorandum. The hearing memorandum identifies six issues for the Commission's consideration. The six issues are, respectively: (1) whether the proposed Salem delivery spur is economically feasible; (2) whether the rates reflected in the transportation agreement between MoGas and Missouri Public Service (MoPub) are appropriate; (3) whether it is appropriate for MoGas to have the ability to flex down from maximum transportation rates on deliveries to MoPub in Salem, Missouri;

(4) whether the MoGas transportation agreement with MoPub usurps the Commission's ratemaking authority and whether certain provisions of the agreement are unlawfully discriminatory; (5) whether the Commission should set an investigatory docket for affiliate transactions; and (6) whether restrictions should be placed upon the certificate, if it is granted.

The evidentiary hearing was held on June 29, 1995. The hearing memorandum and testimony of all witnesses were admitted into the record at the evidentiary hearing.

### **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.

MoGas operates a regulated intrastate natural gas transmission system in the state of Missouri beginning at the interconnect at Sullivan, Missouri, with Missouri Pipeline Company, continuing to Fort Leonard Wood, Missouri. In January of 1995, UtiliCorp United Inc. (UtiliCorp) purchased a 218-mile intrastate natural gas pipeline system in Missouri from Edisto Resources Corporation. UtiliCorp's purchase included Missouri Gas Company and Missouri Pipeline Company as well as the distribution system at Fort Leonard Wood, Missouri. UtiliCorp is an electric and natural gas utility company with December 31, 1994, total assets in excess of \$3 billion. UtiliCorp's 1994 Stockholder's Annual Report indicates that on a consolidated basis, UtiliCorp had \$91.4 million of earnings available for common shares during calendar year 1994. The annual report indicates a capital budget for 1995 of \$38 million for gas operations including pipe replacement and system extensions. UtiliCorp estimates construction expenditures through 1999 to average \$40 million per year. The company has approximately 1.2 million utility customers and 4,700 employees.

The intrastate natural gas transmission system is managed and operated by UtiliCorp Pipeline Systems, a wholly-owned subsidiary of UtiliCorp. The staff of UtiliCorp Pipeline Systems consists primarily of former employees of Edisto's Missouri Pipeline Company and Missouri Gas Company. UtiliCorp also operates a natural gas distribution system known as Missouri Public Service.

In its application and testimony, MoGas proposes building a six-inch (6") line from the existing MoGas ten-inch (10") line at a point northwest of Rolla, Missouri, in the southeast quarter of Section 19, Township 38N, Range 7W in Phelps County to a point just west of Salem, Missouri, at the intersection of Highway 72 and County Road "J" near the center of Section 14, Township 34N, Range 6W in Dent County, Missouri. MoGas estimates that the Salem delivery spur will cost approximately \$2,905,000 to build. The evidence suggests that UtiliCorp will finance the proposed Salem delivery spur from internally generated funds. The actual construction is planned for the third quarter of 1995 with a target operational date of the fourth quarter of 1995.

## **I. Certificate of Convenience and Necessity**

An applicant for a certificate of convenience and necessity must meet three criteria: (1) the applicant must be qualified to provide the proposed service; (2) there must be a need for the service; and (3) the service must promote the public interest.

As stated above, the Commission must consider whether MoGas is qualified to provide the proposed service.

There is no dispute as to whether MoGas is qualified to provide the proposed service. The hearing memorandum states: "All parties stipulate and agree that, from an operational and financial standpoint, MoGas is qualified to provide the service which it proposes by way of its application." (Ex. 1, p. 3).

The Commission finds that Missouri Gas Company is qualified to provide the proposed service and financially capable of constructing, maintaining and operating the proposed Salem delivery spur.

The Commission must consider whether there is a public need for the proposed service.

The Staff does not appear to take a position on whether there is a public need for the proposed service.

The position of MoGas is that there is a public need for the service. Mr. Clark Leonard, Mayor of Salem, Missouri, filed testimony in this proceeding. Mr. Leonard states that in 1990 Salem had a population of approximately 4,500, while Dent County had a population of approximately 14,300. He states that there are approximately 2,050 households in Salem. Mr. Leonard states that approximately 3,500 persons are located within the Spring Creek Township outside of the current city limits, most of which 3,500 persons are potential users of natural gas.

Mr. Leonard states that he expects Salem to continue its population growth of about three percent per year. Mr. Leonard states that unemployment in the Salem area is about 8.5 percent. Mr. Leonard states his belief that many citizens will convert to natural gas given the opportunity. He points out that approximately 80 percent of the voters in the November 1994 general election supported another energy choice by approving the granting of a municipal franchise to Missouri Public Service.

Mr. Leonard states that there is a need for natural gas service in Salem and in the surrounding area. He further states that natural gas as an energy option will promote the overall quality of life in the area and will contribute to economic expansion. He further points out that in order for Missouri Public Service to provide natural gas to Salem, the MoGas transmission

line is necessary and thus, he states, there is a public need for the MoGas transmission line.

The testimony of Mr. Leonard is not contradicted by any party. The Commission finds that Mr. Leonard's statements about the population of Salem, Missouri, anticipated growth in the area, and the impact of natural gas on the overall quality of life and economic expansion is credible evidence as to the public need for the proposed service.

The Commission finds that there is a public need for natural gas in Salem, Missouri, because there is a significant population that can utilize natural gas and the availability of natural gas will be beneficial to the economic growth of Salem and the surrounding area. In addition, the Commission finds that there is a public need for the proposed Salem delivery spur since gas must be transported to Salem to serve that area.

The Commission must also consider whether the proposed service promotes the public interest. The Staff suggests that granting a certificate of convenience and necessity which authorizes construction and operation of the proposed Salem delivery spur does not promote the public interest and, thus, the Commission should deny the request for a certificate. As further discussed in the Conclusions of Law, the Commission concludes that it need not find that a project will be financially viable or profitable in order to grant a certificate of convenience and necessity. However, the Commission must use reasonable efforts to prevent the general body of ratepayers from bearing the costs associated with financially unwise actions by utilities.

The Commission does not intend to suggest that feasibility is irrelevant in connection with applications for certificates of convenience and necessity. For instance, if evidence shows that an applicant is not financially or technically capable of completing the proposal identified in the application,

the Commission would find that the applicant is not qualified to provide the proposed service and, thus, deny the application.

The Commission finds that the proposed Salem delivery spur promotes the public interest because there is a significant population that can utilize natural gas and the availability of natural gas will be beneficial to the economic growth of Salem and the surrounding area. In addition, the Commission finds that construction of the proposed Salem delivery spur promotes the public interest since gas must be transported to Salem to serve that area.

## **II. Other Issues**

### **A. Economic Feasibility**

The Staff's position is that construction of the Salem spur is not economically feasible and not in the public interest because when representative costs of service over the spur are combined with other appropriately developed costs of providing natural gas service to Salem, the total cost of natural gas greatly exceeds the cost of the major competitive fuel, propane. Staff believes that the MoGas rates contained in its transportation agreement with MoPub cannot appropriately be used to set the rates on the Salem spur and to determine the economic feasibility of the spur.

MoGas's position is that if the MoPub Salem proposal, which is the subject of GA-95-216, is not economically feasible and the Commission denies that application, the proposed Salem delivery spur is not feasible because there would be no need for the gas transmission pipeline which is the subject of this case. If, however, the Commission determines that the MoPub application is economically feasible and grants the requested authority to MoPub in GA-95-216, then the Salem spur application is also needed and is economically feasible and should also be granted.

The Commission's legal analysis of this issue is contained in the Conclusions of Law section of this Report And Order. The Commission is of the opinion that neither the estimates of gas transportation volumes provided by the Staff nor the estimates of gas transportation volumes provided by MoGas are unreasonable. The Commission is not inclined to make specific findings regarding the various volume estimates proffered in this proceeding because such findings would not bear upon whether granting the certificate is in the public interest. The Commission's obligation in this regard is to ensure that the general body of ratepayers does not bear the financial burden associated with the uneconomic decisions of utilities. This function is accomplished through ratemaking proceedings rather than through certificate proceedings. This point is discussed further in the Conclusions of Law section of this Report And Order.

## **B. Transportation Rates**

Staff's position is that the Commission should order the use of an add-on spur rate in addition to the existing mainline rates. Staff argues that this will help assure that those customers using the spur are held responsible for the recovery of the costs related to the spur. Staff's proposal is that the aggregate rate charged customers provided service by the spur should consist of: (1) a rate which recovers the cost to serve customers on the spur, plus (2) the rates already approved for the use of the MoGas mainline.

Staff witness Hubbs developed a rate which Staff believes would recover the costs of the spur in an appropriate manner. Mr. Hubbs used the spur's cost of service level developed by Staff witness Winter and divided it by the Staff's estimated level of gas sales. Staff witness Flowers developed the Staff's estimate of gas sales.

Mr. Hubbs developed the spur rate using traditional ratemaking with the costs of the spur and the MoGas sales volumes expected after completion of

the project. The spur rate, generated using Staff's estimated costs and sales volumes, is \$3.16 per Mcf of transported gas. This rate, in Staff's view, represents the rate needed to recover the cost of service using the Company's cost and sales figures.

Staff's position is that MoGas should not be allowed to flex its transportation rate down for service provided on the spur. Staff's view is that flexing down for an affiliate for service over the spur could distort the feasibility of both systems, MoGas and MoPub. Staff recommends that the proposed Salem delivery spur be required to stand on its own by requiring the cost related to the spur be recovered from MoPub by charging the full rate of \$3.16 per Mcf for all service on the spur.

MoGas is opposed to the establishment of special cost-based rates for the Salem delivery spur. Instead, MoGas believes that it is in the public interest for it to be able to provide transportation service in accordance with its existing rates, which have been filed and approved and authorize a maximum charge and permit a discount or flexdown below the maximum rate.

The Commission finds that there is no compelling reason to restrict MoGas' ability to discount or flex transportation rates. MoGas is engaged in the transportation of natural gas on an intrastate basis. The Commission is of the opinion that MoGas's filed and approved transportation rates should apply on a system-wide basis. The Commission will not treat the MoGas system in a piecemeal fashion. If there is a problem with the existing MoGas transportation tariffs, then Staff may bring that problem to the Commission's attention by way of a complaint filing.

Although the Commission will not attempt to preclude MoGas from providing discounted transportation service, this is not intended to suggest any ratemaking treatment. Transactions between affiliated companies warrant intense regulatory scrutiny, and the Commission will order MoGas to separately account

for expenses related to the Salem delivery spur to ensure that transactions between MoGas and MoPub are subject to that scrutiny.

**C. MoGas Transportation Agreement With MoPub**

The Staff alleges that the transportation agreement in effect between MoGas and MoPub is unlawfully discriminatory. Staff believes that a provision in the agreement requiring MoGas to adjust transportation rates to be competitive with the delivered price of propane is discriminatory. Staff suggests that the Commission should require MoGas to make this same offer to all its transportation customers.

MoGas denies that the agreement is unlawfully discriminatory.

The Commission does not see any evidence in the record of this case to suggest that MoGas has engaged in unlawful conduct. If the Staff believes that MoGas engages in unlawful, discriminatory practices in the future, the Staff should consider filing a complaint on that basis and offer evidence of such conduct.

While the Commission has given serious consideration to the arguments of the Staff, this matter turns on a basic consideration of utility regulation. It has long been the Commission's policy that it is unwise to attempt, through regulation, to manage the business affairs and decisions of the investor-owned utilities which it regulates, so long as the ratepayers are protected from potential abuses by the monopoly provider. In this regard, while MoGas and MoPub may engage in activity that is detrimental to the general body of ratepayers, no subsidy by the ratepayer will occur until and unless those excess costs are built into the rate structure, either through a rate case or the PGA/ACA process. The Commission will, therefore, allow MoGas to perform under the contract.

#### **D. Investigatory Docket for Affiliate Transactions**

The Staff has requested that the Commission open a docket to investigate affiliate transactions of MoGas.

MoGas has indicated no objection to the establishment of a docket to investigate affiliate transactions.

The Commission finds that the establishment of such a docket is not warranted. The Staff already has investigatory powers under Missouri law. The Staff is free to use that power and pursue filing a complaint if Staff determines that such action is warranted.

#### **E. Restrictions on Certificate**

The Staff requests that the certificate granted to MoGas be limited so that MoGas cannot bypass municipalities, regulated local distribution companies (LDCs) or the federal government. In response to Staff's concern the Commission makes the following observation. The certificate granted to MoGas by this order is a certificate for the transmission of natural gas. The original certificate granted to MoGas in GA-90-280 is for the transmission of natural gas.

The Commission hereby takes official notice of the Report And Order it issued in GM-94-252. In that order, the Commission stated: "The Commission finds that the certificates issued, and which will be passed to UCU [UtiliCorp] 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." (Report And Order, p. 11). To clarify this point, the Commission concludes that MoGas must obtain Commission authorization to provide any other service from this line.

The certificate possessed by MoGas is not a service area certificate. Rather, the certificate possessed by MoGas is a certificate for the transmission

of natural gas. If an entity wishes to provide local distribution service, that entity must apply for a service area certificate with the Commission.

The Commission finds that the same limitations apply to the certificate granted hereby as the limitations applicable to the original MoGas certificate issued in GA-90-280.

### **Conclusions of Law**

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

The Commission has jurisdiction over this application under Section 393.170, R.S.Mo. 1994. Section 393.170 states the Commission has the power to grant a certificate of public convenience and necessity whenever it shall, after due hearing, determine that granting the certificate is necessary or convenient for the public service.

The Commission is of the opinion that Staff's argument about economic feasibility is based upon an incorrect premise. The premise is that the Commission must determine economic feasibility with respect to individual gas transmission line extensions. In a legal sense, the essence of Staff's position is that the Commission must conclude that granting a gas transmission line certificate is not in the public interest unless the applicant can prove that the project will be economically feasible on a stand-alone basis. This premise is not consistent with ratemaking using historical test year principles.

The evidence provided by Staff about economic feasibility does not lead the Commission to the conclusion that the certificate is not in the public interest. The Commission is of the opinion that neither the estimates of gas transportation volumes provided by the Staff nor the estimates of gas transportation volumes provided by MoGas are unreasonable. These are just estimates. The Commission's obligation is to ensure that the general body of ratepayers does not

bear the financial burden associated with imprudent, uneconomic decisions by utilities. This function is best performed in the context of a rate proceeding where the utility's authorized rate base is audited and reviewed. One result of the Staff's position on the economic feasibility issue is to put MoGas on notice of the potential for a proposed disallowance from rate base of what a party may view as an imprudent investment or expenses associated with the investment in the context of a future rate or complaint proceeding.

The Commission continues to agree with the three criteria for granting a certificate of convenience and necessity which were stated in GA-89-126 (initial application for a certificate by Missouri Pipeline Company) and followed in GA-90-280 (Intercon Gas, Inc.). The three criteria, as articulated in these previous Commission Reports And Orders, are: (1) the applicant must be qualified to provide the proposed service; (2) there must be a need for the service; and (3) the service must promote the public interest.

It has been established in the Findings of Fact that Missouri Gas Company is qualified and financially able to construct, operate and maintain the proposed gas transmission extension. Furthermore, it has been established in the Findings of Fact that there is a public need for natural gas service in Salem, Missouri. The Commission has concluded in its decision in GA-95-216 issued this day that the provision of natural gas to the citizens of Salem, Missouri, promotes the public interest. This proposed gas transmission extension is necessary to deliver natural gas to Salem, Missouri. Thus, the proposed Salem delivery spur promotes the public interest. The Commission concludes that the proposed extension of the gas transmission system of Missouri Gas Company is necessary and convenient for the public service. Therefore, the Commission will grant a certificate of convenience and necessity to Missouri Gas Company authorizing the proposed Salem delivery spur.

The Commission also concludes that the currently filed and approved rates and charges of Missouri Gas Company shall apply to this proposed extension. The Commission is not persuaded by Staff's argument that a special cost-based surcharge for this gas transmission line extension is warranted. The Commission finds that neither the City of Salem nor the Salem delivery spur should be treated as a discrete area upon which to set cost-based rates because this would contradict the Commission's policy of keeping downstream deliveries of natural gas at a competitive level. *In re Intercon Gas, Inc.*, 30 Mo. P.S.C. 554, 565; *In re Missouri Pipeline Company*, Case No. GA-92-314, Report And Order, p. 6.

Notwithstanding the Commission's conclusion in this matter that discrete rate areas are not warranted, the Commission makes the following observation. The Commission shares the Staff's concern insofar as there is the potential that the costs of uneconomic decisions by utilities may be spread to the general body of ratepayers. It appears to the Commission that if a utility makes what would be, in an unregulated marketplace, poor business decisions and takes uneconomic actions based on those decisions, the general body of ratepayers should not have to bear the financial burden associated with such uneconomic actions. The Commission concludes that a regulatory regime whereby MoGas and MoPub are allowed to engage in destructive price competition to drive out propane in given markets and then force the general body of ratepayers to bear the expense of the destructive competition through cross-subsidization from the firm's more lucrative geographic areas, is not in the public interest. It appears that if expenditures incurred by MoGas or UtiliCorp to provide natural gas to Salem, Missouri, or any other area prove to be unreasonable or imprudent, then shareholders rather than ratepayers should bear the cost associated with the uneconomic action. This could be accomplished through adjustments to rate base in the context of a rate proceeding.

The Staff requests that the Commission preclude MoGas from flexing transportation rates to a level below the maximum transportation rate authorized by its tariff. The Commission is of the opinion that this is an issue most appropriately addressed in a rate or complaint proceeding. The Staff may choose to recommend transportation rates for MoGas using the maximum transportation rate applied to estimated volumes (i.e., impute revenues at full transportation rate for revenue requirement calculations). One question that may arise in the context of this ratemaking issue would be whether the Company's efforts to compete with propane are a legitimate basis upon which to flex down. However, since this proceeding does not involve ratemaking determinations, the Commission need not address the issue at this time.

**IT IS THEREFORE ORDERED:**

1. That Missouri Gas Company is hereby granted a certificate of public convenience and necessity to construct, install, own, operate, control, manage and maintain a 28-mile natural gas transmission pipeline and related facilities originating at a point near Rolla, Missouri, and proceeding in a generally south/southeasterly direction through Phelps and Dent Counties, Missouri, to a point near Salem, Missouri.

2. That Missouri Gas Company shall file tariff sheets which contain a concise description and map showing the route of the pipeline herein authorized, such tariffs to become effective no later than thirty (30) days after completion of construction.

3. That Missouri Gas Company shall file tariff sheets which contain the legal description of this extension no later than thirty (30) days after completion of construction.


4. That nothing in this order shall be considered as a finding by the Commission of the value for ratemaking purposes of the properties herein

involved, nor as an acquiescence in the value placed upon said properties by Missouri Gas Company. Furthermore, the Commission reserves the right to consider the ratemaking treatment to be afforded these transactions in any later proceeding.

5. That UtiliCorp United Inc. and Missouri Gas Company shall keep a separate and complete accounting of costs associated with the Salem delivery spur and will provide that separate accounting to the Staff upon proper request in any future rate of complaint proceeding.

6. That this Report And Order shall become effective on the 18th day of August, 1995.

**BY THE COMMISSION**



**David L. Rauch**  
**Executive Secretary**

( S E A L )

Mueller, Chm., McClure, Kincheloe  
and Crumpton, CC., concur and certify  
compliance with the provisions of  
Section 536.080, R.S.Mo. 1994.  
Drainer, C., not participating.

Dated at Jefferson City, Missouri,  
on this 8th day of August, 1995.