

**STATE OF MISSOURI
PUBLIC SERVICE COMMISSION
JEFFERSON CITY**

October 9, 2001

CASE NO: GM-2001-585

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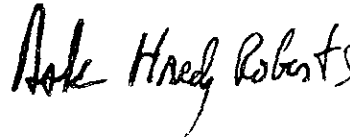
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Enclosed find certified copy of an REPORT AND ORDER in the above-numbered case(s).

Sincerely,



**Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge**

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



In the Matter of the Joint Application of
Gateway Pipeline Company, Inc., Missouri
Gas Company and Missouri Pipeline Company
and the Acquisition by Gateway Pipeline
Company of the Outstanding Shares of
UtiliCorp Pipeline Systems, Inc.

Case No. GM-2001-585

REPORT AND ORDER

Issue Date: **October 9, 2001**

Effective Date: **October 18, 2001**

101

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Gas Company and Missouri Pipeline Company
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Case No. GM-2001-585

APPEARANCES

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and

MICHAEL C. PENDERGAST and **JOSEPH T. CLENNON**, 720 Olive Street, St. Louis, Missouri 63101, for Laclede Gas Company.

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REGULATORY LAW JUDGE: Keith A. Thornburg

REPORT AND ORDER

Syllabus

This Report and Order grants an application authorizing Gateway Pipeline Company, Inc. (Gateway) to buy all the shares of UtiliCorp Pipeline Systems (UPL) under a Stock Purchase Agreement with UtiliCorp United Inc. (UtiliCorp). The Commission determines that, subject to the conditions imposed herein, the transaction is not detrimental to the public interest.

As a result of this transaction, Gateway will acquire control and indirect ownership of Missouri Pipeline Company (MPC) and Missouri Gas Company (MGC). MGC and MPC are subsidiaries of UPL and indirect subsidiaries of UtiliCorp. MGC and MPC are Missouri regulated public utilities that own separate but connected intrastate natural gas transmission pipelines crossing east, east central, and south central Missouri. Gateway will also acquire control of an inactive interstate pipeline extending from Missouri under the Mississippi River into Illinois, referred to as the Trans Mississippi Pipeline (TMP).

Jurisdiction

The Commission's jurisdiction was contested in this matter. On May 24, 2001, the Commission issued its order determining that it has jurisdiction in a 3 -1 decision and joined UtiliCorp as a necessary party. The Commission summarizes the basis for its jurisdiction here.

The Public Service Commission is a body of limited jurisdiction and has only such powers as are expressly conferred upon it by the Statutes and powers reasonably

incidental thereto. *State ex rel. and to Use of Kansas City Power & Light Company v. Buzard*, 168 S.W.2d 1044, (Mo. Banc 1943). Under Section 386.250(1) and (5), the Commission has jurisdiction extending to the distribution of natural gas within the state and to all public utility corporations subject to the Public Service Commission law. UtiliCorp is the seller in the agreement presented for the Commission's approval. UtiliCorp is both a gas and an electrical corporation under Section 386.020. UtiliCorp is a public utility and is subject to the jurisdiction of the Commission.

Under Section 393.190(1) no gas corporation may sell or otherwise dispose of any part of its works or system nor by any means, direct or indirect, merge or consolidate such works or system with any other corporation without first obtaining the order of the Commission authorizing it to do so. In this case UtiliCorp, a regulated public utility, is selling its wholly owned affiliate that in turn owns two Missouri regulated public utility companies, MPC and MGC, that each own a state regulated intrastate gas transmission pipeline. UtiliCorp is effectively selling part of its system by selling its wholly owned subsidiaries.

In this case the seller, UtiliCorp, is a regulated public utility corporation. The subsidiaries, MGC and MPC, are also regulated public utilities and are wholly owned and controlled by UtiliCorp through UPL. The transaction presents the sale of part of UtiliCorp's system and therefore the Commission has jurisdiction and a duty to review the transaction and determine whether it may be approved.

Standard of Review

Pursuant to Commission Rule 4 CSR 240-2.060(7) and/or (12), the applicants must show why the proposed transaction is not detrimental to the public interest. The right to sell property is an important incident of the ownership thereof and "[a] property owner should be allowed to sell his property unless it would be detrimental to the public." *State ex rel. City of St. Louis v. Public Service Commission*, 335 Mo. 448, 459, 73 S.W.2d 393, 400 (Mo. banc 1934). "The obvious purpose of [Section 393.190] is to ensure the continuation of adequate service to the public served by the utility." *State ex rel. Fee Fee Trunk Sewer, Inc. v. Litz*, 596 S.W.2d 466, 468 (Mo. App., E.D. 1980). To that end, the Commission has previously considered such factors as the applicant's experience in the utility industry; the applicant's history of service difficulties; the applicant's general financial health and ability to absorb the proposed transaction; and the applicant's ability to operate the asset safely and efficiently. See, *In the Matter of the Joint Application of Missouri Gas Energy et al.*, Case No. GM-94-252 (*Report and Order*, issued October 12, 1994) 3 Mo.P.S.C.3d 216, 220.

Under the pleading presenting the transaction between Gateway and UtiliCorp for the Commission's approval, the moving parties assert that the transaction presented will not be detrimental to the public. Therefore, they have the burden of proving that assertion. *Anchor Centre Partners, Ltd. v. Mercantile Bank, N.A.*, 803 S.W.2d 23, 30 (Mo. banc 1991); see also *Dycus v. Cross*, 869 S.W.2d 745 (Mo. banc 1994).

While UtiliCorp and Gateway must prove that the transaction is not detrimental to the public, other parties have asserted that the merger is detrimental in one or more specific areas. The burden of proof is never shifted; however, the burden of going forward

with evidence may shift if a prima facie case is made. *Anchor Centre Partners* at 30. Therefore, the parties asserting that the merger is detrimental to the public in a particular way have the burden of going forward by presenting sufficient evidence to support their particular assertions.

Procedural History

On April 19, 2001, Gateway Pipeline Company, Inc. (Gateway), Missouri Gas Company (MGC), and Missouri Pipeline Company (MPC) filed a joint application with the Commission seeking either a determination that the Commission is without jurisdiction or, in the alternative, authorization on an expedited basis, for Gateway, to acquire the outstanding shares of UtiliCorp Pipeline Systems (UPL). The application presented a copy of the Stock Purchase Agreement for the proposed transaction. The applicants also requested a protective order to limit access to highly confidential or proprietary business information.

Under the Stock Purchase Agreement, UtiliCorp is selling, and Gateway is buying, all the outstanding shares of the capital stock of UPL. UPL is, according to the application, the parent and owner of MGC and MPC. UtiliCorp, MPC and MGC are regulated Missouri public utilities. MGC and MPC own and operate intrastate natural gas transmission pipelines in Missouri. UtiliCorp was not a party to the application filed on April 19, 2001.

The Commission issued an order on May 2, 2001, directing the Staff of the Missouri Public Service Commission to file its response concerning jurisdiction. Further responses or any reply to the Staff memorandum were due not later than ten days after the

Staff response. The Commission also issued a protective order pursuant to the request by the applicants.

Staff filed its response on May 11, 2001. The Office of the Public Counsel filed its response regarding jurisdiction on May 1, 2001. The applicants filed their reply on May 18, 2001.

On May 24, 2001, the Commission issued an order under a 3-1 vote finding that it had jurisdiction. The order joined UtiliCorp as a necessary party. The Commission ordered the parties to file a tax impact statement showing how the transaction would impact tax revenues of political subdivisions in Missouri. The order also directed notice to counties traversed by the intrastate gas transmission pipelines of MPC and MGC and to the identifiable municipalities and companies owning and operating natural gas distribution systems served by the transmission pipelines. The order provided for public notice of this proceeding.

On June 1, 2001, Gateway's attorneys entered their appearance on behalf of UtiliCorp. Subsequently, on June 14, these attorneys filed a notice withdrawing as counsel for Gateway, noting the entry of a different law firm to represent Gateway's interests. The Commission granted leave for the withdrawal on June 15.

A tax impact statement was filed by Gateway, MPC and MGC on June 5, 2001, stating that the transaction would have no tax impact on the tax revenues of the political subdivisions in which any structures, facilities or equipment of MPC or MPC are located. On June 11, 2001, the Commission provided the tax impact statement to the parties and to the county clerks for Pulaski, Phelps, Crawford, Franklin, St. Charles, Lincoln and Pike Counties.

On June 11, 2001, the Commission granted the intervention requests of Union Electric Company, d/b/a AmerenUE, Laclede Gas Company (Laclede) and Panhandle Eastern Pipeline Company. No other intervention requests were filed.

Prehearing conferences were held on June 28 and August 1 and 15, 2001. Prefiled direct, rebuttal and surrebuttal testimony, with schedules and exhibits and supplemental testimony, were filed in this case in accordance with usual Commission procedures and pursuant to orders entered in this case.

The Office of the Public Counsel moved the Commission to reclassify some of the highly confidential and proprietary information provided in discovery and in testimony in motions filed on August 1, 7 and 14, 2001. Gateway responded in opposition. On August 28, 2001, the Commission issued its Order Regarding Classification of Responses to Data Requests resolving the classification issues. On August 30, 2001, Gateway requested a clarification regarding proprietary information presented in the text of a data request. On September 25, 2001, the Commission issued an order granting the clarification requested by Gateway.

The hearing for this case was held beginning on September 5 and ending on September 7, 2001. One round of briefs was ordered and was filed on September 18, 2001. Some parties submitted proposed findings of fact and conclusions of law. One party, Panhandle Eastern, elected not to file a brief.

On September 18, 2001, the Municipal Gas Commission, for itself and for the Cities of Cuba, Richland, St. James, Sullivan and Waynesville, Missouri, and for Fidelity Natural Gas, Inc., filed a motion requesting leave to file an amicus brief and also filed their amicus brief with their motion.

On September 24, 2001, UtiliCorp filed an objection to and motion to strike a portion of the brief filed by the Commission's Staff. Staff filed a reply to UtiliCorp's motion on October 1, 2001.

Positions of the Parties

In the application filed on April 19, 2001, Gateway, MPC and MGC asserted that the proposed transaction is not detrimental to the public interest because: 1) the status of MGC and MPC as wholly owned subsidiaries would not change; 2) there will be no change in the operations of MGC or MPC and these companies will continue to provide service to their customers pursuant to the rates, rules, regulations and other tariff provisions of MGC and MPC currently on file with and approved by the Commission until such time as they may be modified according to law; 3) the existing customers of both MGC and MPC will continue to experience quality day-to-day utility service at approved rates and the transaction will be entirely transparent to them; and 4) the Commission will retain full authority to regulate the rates and terms and conditions of service rendered by MGC and MPC as provided by law.

The Commission's Staff, the Office of the Public Counsel and Laclede all opposed approval of the transaction. This opposition was based upon the assertion that the pipeline operations of MPC and MGC have not been profitable on an after-tax basis; and that Gateway lacks the financial resources and a detailed business plan to support and improve the performance of the pipeline operations to assure continued operation without interruption or significant pricing or service changes. These parties also were critical of the management performance of one of the principals in the ownership structure.

These parties asserted that additional costs of the proposed equity and debt structure and costs for expansion of services would be detrimental to Missouri customers resulting in potential service disruptions or a re-bundling and re-pricing of services imposing higher costs for existing services.

These parties were also concerned that aspects of Gateway's business plan would make it more likely that the Commission would lose its jurisdiction over MPC and MGC to the Federal Energy Regulatory Commission (FERC). The parties asserted that changes in regulatory perspectives from a state to federal level and that changes in rate case procedures would be detrimental to Missouri customers.

Because FERC jurisdiction arose as an issue, Gateway has requested a clarification of a restriction in MPC's certificate of service authority regarding the interconnection of MPC's pipeline with the TMP.

AmerenUE expressed "concerns" with the transaction that mirrored those of other parties but did not take a position in support or opposition to the proposed transaction. Panhandle Eastern Pipeline (Panhandle) did not take a specific position and did not file a brief.

Conditions were offered by Staff and by Laclede assuming the Commission approved the transaction. AmerenUE concurred in the recommended conditions.

Findings of Fact

The Missouri Public Service Commission makes its findings of fact having considered all of the competent and substantial evidence upon the whole record. The positions and arguments of all of the parties have been considered in making this decision.

Failure to specifically address a piece of evidence, position or argument of any party does not indicate that the Commission failed to consider relevant evidence, but indicates rather that the omitted material was not dispositive of this decision.

**Companies and Utility Facilities Presented in the Application
and in the Stock Purchase Agreement:**

The Joint Applicants in the case are Gateway, MPC and MGC. Gateway is a Delaware corporation with offices located in Littleton, Colorado. Gateway is authorized by the state of Missouri to do business in the state as a foreign corporation. Gateway currently conducts no business in the state of Missouri, or elsewhere. It has been created for the specific purpose of acquiring UPL.

UPL is a wholly owned subsidiary of UtiliCorp. UtiliCorp is a Delaware corporation doing business in the state of Missouri. It provides regulated electric and natural gas utility service to customers in the state of Missouri in those areas certificated to it by the Commission. Pursuant to an order dated May 24, 2001, UtiliCorp was determined to be a necessary party to a full adjudication of the issues presented by the Joint Application. Consequently, the Commission added UtiliCorp as a party to the proceeding.

MPC and MGC are both Delaware corporations. Both companies are engaged in owning and operating natural gas transmission pipelines in the state of Missouri subject to the jurisdiction of the Commission as provided by law. The Commission granted the companies Certificates of Convenience and Necessity in its Case Nos. GA-89-126, GA-90-280, GA-90-276, GA-91-81 and GA-91-82. MPC and MGC are wholly owned subsidiaries of UPL.

MPC transports natural gas for its shippers from a point of interconnection with Panhandle near Curryville, Missouri, in Pike County to several delivery points on the system in the counties of Pike, Lincoln, St. Charles and Franklin to a point of termination in Sullivan, Missouri. The interconnection with Panhandle is MPC's sole intake point for gas delivery.

Generally, MPC transports natural gas on behalf of shippers to requested points along the pipeline system. MPC's shippers are local (gas) distribution companies (LDCs), municipalities operating gas distribution systems, industrial and large commercial natural gas end users, or natural gas marketing companies moving gas on behalf of LDCs, municipalities or natural gas end users behind the LDCs or municipal systems. MPC has ten different delivery interconnects with Laclede, Union Electric Company, Missouri Natural Gas Company and Fidelity Natural Gas. It also has one interconnect with its sister pipeline, MGC, near Sullivan, Missouri.

MGC transports natural gas for its shippers from a receipt point at its interconnect with MPC to several delivery points along its system in the counties of Crawford, Phelps and Pulaski to its point of termination at Fort Leonard Wood, Missouri. The interconnection with MPC is MGC's sole source of transport to its delivery system.

MGC's shippers are LDCs, municipalities, industrial and large commercial natural gas end users, or natural gas marketing companies moving gas on behalf of LDCs, municipalities, or natural gas end users behind the LDCs or municipal systems. MGC has eight delivery interconnects. Three of those are with an LDC, Missouri Public Service (MPS), a division of UtiliCorp, at Rolla, Salem and Owensville. MGC also has delivery

interconnects with the municipalities of Cuba, St. James, St. Robert and Waynesville. MGC also delivers natural gas to Fort Leonard Wood.

Schedule 2-1 to Exhibit 16 (rebuttal testimony of James Gray) is a map that shows MPC's interconnection with Panhandle's interstate pipeline in Pike County. MPC's system traverses four Missouri counties: Pike, Lincoln, St. Charles; and Franklin. The map shows MPC pipeline's southernmost point where it interconnects with MGC's pipeline in Franklin County. MGC's pipeline traverses four Missouri counties: Franklin, Crawford, Phelps and Pulaski. MGC has lateral pipelines that enter the Missouri counties of Gasconade and Dent. Presently all the public utility activities of MPC and MGC occur and are regulated on an intrastate basis.

In addition to holding all of the capital stock of MPC and MGC, UPL also owns a short length of pipe crossing under the Missouri River from Illinois into Missouri, which has been referred to as the Trans Mississippi Pipeline (TMP). The TMP is approximately six (6) miles of pipeline stretching from West Alton, Missouri, under the Mississippi River and into Illinois. The TMP is not currently activated for service. It is physically disconnected from the MPC pipeline.

The Transaction:

According to the terms of a Stock Purchase Agreement entered on April 21, 2001, UtiliCorp has agreed to sell, and Gateway has agreed to buy, all the issued and outstanding shares of the capital stock of UPL. The Stock Purchase Agreement was filed with the application and was also attached as Schedule RCK-4 to the direct testimony of Richard C. Kreul. A diagram marked as Schedule RCK-3 to the direct testimony of Mr. Kreul shows the current and proposed ownership of MPC and MGC. Essentially,

Gateway replaces UtiliCorp as the parent of UPL and thus as owner through UPL of MPC and MGC. Gateway, through its acquisition of UPL, will also acquire the TMP.

Under the terms of the Stock Purchase Agreement, Gateway will pay \$63.4 million to buy all the UPL stock. The agreement attributes \$53.1 million of the purchase price to the net book value for the regulated pipeline assets of MPC and MGC (\$32.7 and \$20.4 million respectively), plus \$10.3 million for the remaining assets consisting of the TMP.

A. Source of borrowed funds and terms.

Gateway will finance the purchase using the proceeds of a term loan secured by UPL stock plus the proceeds of an equity investment or subordinated loan from Gateway's parent Mogas Energy LLC (Mogas).

Gateway's lender is identified as Banc One Capital Markets, Inc. (or as a syndicate headed by Banc One). The loan from Banc One will fund a substantial portion of the purchase price Gateway is paying under the Stock Purchase Agreement. All the stock of UPL will be pledged to secure this loan.

Loan terms require Mogas to make an equity investment in Gateway or loan Gateway sufficient funds to pay the remainder of the purchase price set in the Stock Purchase Agreement, and pay all expenses related to the purchase, and, to provide working capital satisfactory to Banc One. Banc One's security interest is superior to all other interests including the debt or equity interest of Mogas. The assets of Gateway or its subsidiaries cannot be encumbered by any lien or sold without Banc One's consent with the exception of limited occurrences in the usual course of business. Gateway cannot

merge or consolidate and may not engage in transactions with affiliates that are not on an arms-length basis.

The loan terms impose certain financial covenants on Gateway such as requiring maintenance of financial coverage and performance ratios and funding of a Reserve Account. Gateway must provide its lender un-audited quarterly and audited annual financial reports and must furnish quarterly compliance certificates and other financial information to its lender.

B. Source of invested funds and terms.

Gateway is wholly owned by Mogas Energy, LLC, a Delaware company. Mogas is owned jointly by Mr. Dennis Langley, Mr. David Ries and TCW Group. The principal investors in Mogas will contribute the balance of funds through Mogas necessary for Gateway to complete its acquisition of all the stock of UPL.

TCW is investing the bulk of funds that will fund the Mogas equity investment in Gateway that in turn is a source of funds to purchase UPL stock, pay transaction costs and provide working capital. TCW Group is a privately held investment company.

Mr. Langley will provide significant cash investment through Mogas to Gateway that is a source of funds to purchase UPL stock, pay transaction costs and provide working capital. Mr. Langley is currently president of two development companies and has 20 years' experience as an attorney and executive in the energy industry including pipeline systems.

Mr. Ries is not investing cash in Gateway or Mogas but will receive an equity interest in Mogas in return for his services arranging the transaction and for his management of Gateway and its proposed subsidiaries, MPC and MGC and the TMP.

Mr. Ries will manage the day-to-day operations of Gateway, MPC and MGC. Mr. Ries has 26 years' experience as an engineer, manager and executive in the energy industry primarily with oil and gas pipelines.

At the time of the hearing, details of the equity owners' operating agreement were not finalized or available. However, Mr. Ries' testimony shows that ownership control will rest primarily with Mr. Langley and daily operations and management with Mr. Ries. Initially, TCW will have a higher priority and a larger share in distributions of revenues from the MPC and MGC operations and future TMP revenues. If TCW does not obtain expected returns of and on its investment, its ownership interest in Mogas will increase. If TCW obtains expected returns, its ownership interest in Mogas will gradually decrease and the proportionate interests of Mr. Langley and Mr. Ries will increase.

Operations Following Acquisition:

Gateway intends MPC and MGC to operate and provide services under their existing tariffs and under the jurisdiction and regulation of the Commission. All existing operational procedures and plans will be continued by Gateway. Gateway has agreed to a condition that findings in this Report and Order shall not be considered as findings for ratemaking procedures in any subsequent proceeding.

Mr. Richard C. Kreul, a UtiliCorp Vice President, is currently the president of MPC and MGC. Mr. Kreul provides overall direction and management of MPC and MGC including operations, regulatory compliance, business development and strategic planning. Mr. Kreul is involved in negotiating contract terms with large customers for MPC and MGC. Mr. Kreul holds bachelor and master degrees in mechanical engineering and has more than 20 years' experience in the energy industry and pipeline business. Mr. Kreul will

remain with UtiliCorp after the proposed transaction closes and will not continue with MPC or MGC.

Mr. Kreul's functions will be taken over and carried on by Mr. Ries, a principal in Mogas. Mr. Ries holds a bachelor's degree in civil engineering and has 27 years of engineering and management experience that is comparable to that of Mr. Kreul. Mr. Ries will be the President and Chief Executive Officer of Gateway and will have day-to-day management responsibility for MPC and MGC. No party raised an issue with Mr. Ries' qualifications, ability or character to carry out his responsibilities.

All seven of Gateway's field employees will be offered employment with Gateway. These employees carry out the bulk of the daily and periodic activities of physically operating, maintaining and servicing the pipelines owned by MPC and MGC.

Some MPC and MGC accounting functions are supported by UtiliCorp and these functions will have to be replaced.

Two UtiliCorp employees based in Kansas City handle most negotiations, routine contracting, and scheduling and nomination of pipeline services. These employees will remain with UtiliCorp. These functions will also have to be replaced.

The Stock Purchase Agreement provides a Transitional Services Agreement as Exhibit C and an open ended listing of services to be provided by UtiliCorp as mutually agreed at Schedule 1.1(a). Under the Transitional Services Agreement, UtiliCorp agrees to provide services to Gateway as an independent contractor on a cost plus percentage basis as can be practically accomplished for up to one year after closing.

A concern was expressed that the contracting, negotiation and nominating functions for services were very sensitive and essential to assuring uninterrupted services

during a change of ownership, particularly if the Stock Purchase Agreement were closed during the winter heating season. AmerenUE's witness, Julianne Heins, described this concern and the need to have specific employees designated for these functions. Ms. Heins indicated that AmerenUE has had discussions with Mr. Ries about retaining the services of the current UtiliCorp employees performing these functions under contract through the winter heating season. The administration of nominations as provided by the two employees out of UtiliCorp's Kansas City offices is described as a function that can be included in the Transitional Services Agreement that is included with the Stock Purchase Agreement.

Operational Safety:

Mr. John D. Kottwitz, an engineer in the Commission's Safety and Engineering section, offered three safety related conditions should the Commission approve the transaction presented in the Stock Purchase Agreement as follows: 1) MPC and MGC must follow the pipeline safety regulations as contained in 4 CSR 240-40.020, 40.030, and 40.080; 2) MPC and MGC must continue to use an adequate number of qualified personnel to operate and maintain the pipelines and respond to any emergencies along the pipeline and that these personnel must continue to be qualified in accordance with 4 CSR 240-40.030(12)(D); and, 3) there must be no lapse in the call center, dispatch, emergency response, the Supervisory Control and Data Acquisition (SCADA) system, and gas control functions for MPC and MGC during the transition of ownership. Mr. Kottwitz indicated that Gateway would accept these conditions. Gateway indicated its acceptance of these safety conditions in its brief.

Contested Issues

The Staff, the Office of the Public Counsel, Laclede, and to a limited extent AmerenUE, all took positions that the transaction should not be approved based on financial concerns and concerns with Gateway's management of MPC and MGC. These parties assert that the stock purchase transaction is detrimental to the public interest because the financial circumstances of MPC, MGC and Gateway and the management characteristics of Gateway present a risk that MPC and MGC will fail to provide the service and facilities necessary to deliver natural gas transport services safely and adequately at prices that are just, reasonable and allowable by law and by order of the Commission.

Financial concerns were expressed in the context that MPC and MGC have failed to generate anticipated financial returns under UtiliCorp's ownership. Parties opposed to the transaction assert that Gateway lacks the depth of financial resources to sustain the presently marginal operations of MGC and MPC and that Gateway lacks viable options to improve the profitability of MGC and MPC.

The opposing parties, and particularly the Office of the Public Counsel and Laclede, presented arguments questioning the tenor of management operations under an ownership structure with Mr. Langley as a principal.

Financial Viability – Gateway's Financial Resources:

MPC and MGC do not presently generate favorable returns on equity on an after tax basis. Gateway must have resources to sustain current operations to assure that services are not disrupted. Gateway's application and the testimony of Mr. Ries, Gateway's President and CEO, present a reasonable basis to find that Gateway will sustain the current operations of MPC and MGC.

Gateway has arranged equity and short-term debt financing to obtain approximately \$66 million to pay the stock purchase price of \$63.4 million and allow for additional funds to pay transaction costs and to provide working capital. If current operations were not sustained, Gateway's debt and equity investors would be subject to significant losses. These significant debt and equity investments provide a powerful incentive to these investors to sustain operations without interruption.

The proposed loan terms provide Gateway's lender, Banc One, with considerable oversight of Gateway's financial status, limit Gateway's authority to encumber assets, and provide leverage that could draw equity contributions from one or more of the equity investors to avoid a default and forfeiture of Gateway's stock. In addition the loan is for a short term and will require periodic restructuring and associated review and diligence on Banc One's part.

Under a worst case scenario, described by Mr. Ries, the equity holders could lose their investment. Banc One would acquire the UPL stock and proceed to sell MPC, MGC and the TMP to recover the debt principle. The pipeline systems produce sufficient cash flows to pay operating expenses and interest expense. Their highest value can only be realized by their continued operation. If Gateway defaults on its obligations and suffers a foreclosure, Banc One would have no reason to discontinue MPC and MGC operations and suffer a loss of the cash flow supporting the debt service requirements or otherwise impair its collateral.

Mr. Ries testified that after paying cash expenses that Gateway would willingly use available cash flows, reflecting net income plus depreciation, to cover a return for equity investors. This position shows Gateway's commitment to sustain the operations of

MPC and MGC and meet its expenses and obligations to lenders and to its equity partners even if the return on equity fails to meet expectations.¹

Financial Viability – the Status Quo:

The present operations of MPC and MGC under UtiliCorp's ownership are not generating a significant return on equity and essentially present a break-even business. UtiliCorp is operating these assets as efficiently as possible. Its field operations are appropriately staffed. In addition, the pipelines are subscribed and operated at their present maximum capacity. To obtain maximum throughput volume and revenues, MPC and MGC have had to flex their rates charging less than their tariffs would permit to meet market competition, primarily from propane and other transporters in the St. Louis market.

Gateway proposes to retain all the existing field personnel, bring in a president and CEO with comparable experience and replace present accounting functions and the staff positions responsible for nominations for pipeline transport capacity. Gateway proposes to maintain existing services under existing tariffs. The near term operations and operational expenses of MPC and MGC will not change. Over a longer term, Gateway intends to increase revenues and profitability by increasing throughput volumes and sales while operating within present tariff rates.

Staff has raised a concern that Gateway will attempt to raise prices and that as a result transport volumes could fall leading to a decline in revenues. The market will not change merely because of Gateway's acquisition. Gateway faces the same incentives to maximize revenues as UtiliCorp. Even if Gateway can sustain volumes and obtain higher

¹ The Commission is cognizant that depreciation cash flow also provides a source of funds for reinvestment in assets to assure the long-term viability of a business operation. Using these funds to pay a return on or of an equity investment could impair operations if sustained over a long period of time.

prices, the pricing will still be subject to the tariff limits for MPC and MGC. Inasmuch as the tariff rates are just and reasonable, this transaction does not present a public detriment with respect to pricing.

Gateway provided pro forma financial statements for MGC and MPC projecting an increase in operating revenues. However, if revenues remained static, sufficient revenues would be available to pay operating expenses and to service Gateway's interest expense on debt. Thus, Gateway has the financial resources to sustain the present operations of MPC and MGC without interruption. Gateway's shareholders and lenders are knowingly accepting the risk in acquiring UPL and its affiliates under the circumstances presented that desired returns on equity might not be obtained. Whether or not Gateway and its owners realize a favorable return on their investment, the legal obligation and duty of MPC and MGC to provide safe and reliable public utility service at just and reasonable rates is not diminished.

Financial Viability – Options to Improve Financial Performance:

UtiliCorp through the testimony of Mr. Kreul and Gateway through the testimony of Mr. Ries show a recent development presenting an opportunity for improved financial performance for MPC and MGC.

Presently, MPC's only interconnection to take natural gas into its system is with an interstate pipeline owned and operated by Panhandle. MGC's only interconnection to take natural gas into its system is its sister intrastate pipeline – MPC. LDCs and municipalities and other shippers using MPC and MGC facilities must also contract with Panhandle. In MPC's and MGC's service territories, the final delivered cost of natural gas to an end user must be competitive with propane. MPC's transport costs must be

competitive with other transporters serving St. Louis. Panhandle presently has greater pricing leverage for the transportation component of the cost of gas than MPC or MGC. To maximize revenues by shipping at full capacity, MPC and MGC have discounted their rates to be competitive with propane and other competitors for transporting natural gas.

UPL owns an interstate pipeline, TMP, that crosses from Missouri into Illinois. This pipeline could be connected to MPC under appropriate authority and circumstances. However, excess transport capacity and infrastructure has not been available on the Illinois side of the Mississippi to facilitate gas transport service into Missouri and make interconnection physically or economically feasible.

Natural Gas Pipeline (NGPL) is building a pipeline to transport natural gas into the east Illinois area. This recent development will provide additional transport capacity and infrastructure on the Illinois side of the Mississippi to facilitate gas transport service into Missouri. As many as three interstate pipelines, including Panhandle and NGPL, could be placed in a more competitive status. Interstate pipelines operated by MRT and NGPL presently offer lower transport prices than Panhandle.

MPC and MGC could benefit from a second interconnection in several ways. First, an increase in interstate pipeline capacity would promote price competition and lower upstream shipping costs allowing a margin for MPC and MGC to increase their rates closer to their maximum rates authorized by tariff. End users might see some price decrease or no change.

Second, MPC could become more competitive with other shippers into the St. Louis market and gain volumes in that market.

Third, Gateway, the parent of MPC and MGC, would have an additional source of revenues from TMP to support its debt and equity, relieving some of the operating pressures on these companies.

Fourth, for MPC a second interconnection point could increase its shipping capacity with minimal capital investment. MPC could market additional volumes at or near present prices.

Fifth, greater upstream shipping capacity at lower prices could justify investments in additional compression and other upgrades to increase shipping volume throughout the entire MPC and MGC systems. MPC and MGC could market additional transport volumes at or near present pricing to compete against propane.

Sixth, a second interconnection would enhance service reliability.

Quality of Management Operations:

Laclede, the Office of the Public Counsel and to a lesser extent Staff, all presented concerns with Mr. Langley's holding a controlling ownership interest. These management concerns were based upon Mr. Langley's previous involvement in the ownership and operations of Kansas Pipeline Partnership (KPP). Laclede presented evidence that KPP, in its Kansas pipeline and gas operations, had obtained partial successes in obtaining higher negotiated and contracted rates and had obtained regulatory relief to improve its business profitability, but had done so at the expense of consumers and competitors, and had done so with the additional expenses and burdens of litigation.

Sharp tactics or hard negotiation strategies do not present extraordinary concerns. While the interests of consumers and competitors are often harmonized in

proceedings before the Commission, win-win situations are not always achieved. The evidence presented in this proceeding serves as forewarning to all the parties and the Commission that MPC and MGC may take a more aggressive competitive and regulatory posture in the future. But this evidence does not rise to a level that supports a finding of public detriment.

The record shows further that Mr. Ries rather than Mr. Langley will have day-to-day charge of the business affairs, management and contracting for MPC and MGC. Mr. Ries demonstrated willingness in his testimony to negotiate fairly with any customer and particularly Laclede.

The record shows that MPC and MGC will continue to operate under the same tariffs and Commission rules and regulations after the acquisition as before. Laclede and AmerenUE expressed concern that business practices and customer relationships are not confined solely to terms stated in a utility tariff. However, the tariffs supply the essential terms and prices under which services are provided.

MPC and MGC are established intrastate gas transport companies with an existing client base and not a start-up. In contrast to the issues presented by Mr. Langley's activities in Kansas, problems that may arise with MPC and MGC are more likely to be incremental rather than overwhelming or cascading. The Commission finds that Mr. Langley's ownership interest does not present a detriment to the public.

Commission vs. FERC Jurisdiction:

Every party in opposition to the Stock Purchase Agreement as well as AmerenUE expressed concern with the possibility that the Commission's jurisdiction over

the MPC and MGC pipelines could be lost to FERC and that Missouri's loss of jurisdiction would present a public detriment.

At the present time, MPC and MGC are physically intrastate pipelines and there is no basis for FERC to assert jurisdiction. However, the TMP would be an interstate pipeline under FERC jurisdiction if it were activated. If that pipeline were interconnected with MPC, an affiliate, FERC might assert jurisdiction over MPC and MGC since these pipelines could be viewed as providing interstate service by reason of their affiliated status and interconnection with the TMP.

The parties cited examples of cases presenting affiliate entities where jurisdiction remained with the state and other cases where jurisdiction was taken by FERC. The cases apparently turn on their particular facts.

Under the federal Natural Gas Act, as amended, Section 1(c) provides an exception to federal jurisdiction. A pipeline presenting FERC jurisdictional services can retain its intrastate jurisdictional status if all the gas the pipeline receives from out of state is consumed within the state and the pipeline is regulated by the state commission. This exception is referred to as the Hinshaw exemption.

There are two primary reasons why FERC jurisdiction could be considered a public detriment in comparison to state jurisdiction. First, Missouri and federal rate case procedures differ. In Missouri a tariff filing presenting a rate increase can be suspended pending the Commission's decision and in addition state law sets stringent time limitations for resolving rate cases. In contrast, in federal rate cases a rate increase can go into effect early in the process subject to refund and the cases sometimes take several years to resolve.

Secondly, Missouri has prohibited MPC and MGC from bypassing LDCs and municipal systems. FERC generally allows bypass. Bypass occurs where a transmission pipeline serves a customer directly who would otherwise be served by an LDC. A pipeline may actively market to large users and cause a loss of revenues for LDCs. The LDCs could, in turn, shift fixed costs to other, often smaller consumers, by increasing prices.

Regulatory differences are a factor the Commission should consider. However, offsetting this concern in this case is the fact that an interconnection could greatly improve the poor business performance of MPC and MGC. Furthermore, bringing additional lower cost gas supplies into Missouri could benefit Missouri consumers directly as well as provide the security of an additional source of transport and supply for natural gas.

Gateway has offered a condition that in the event of an interconnection between the MPC and TMP the interconnection would be on a one-way basis only to flow gas into the state and into the MPC system to assure continued state jurisdiction under the Hinshaw exemption.

Connection Restriction Presented in Certificate of MPC:

MPC was originally certificated in 1989. Most of its pipeline assets are converted crude oil pipelines MPC acquired from Amoco. See, Case No. GA-89-126, Report and Order 8-1-89. MGC was certificated in Case No. GA-90-280 (MPC obtained a certificate to build/extend facilities in St. Charles County in this case also). UtiliCorp acquired MPC and MGC in 1994 for \$55.4 million - subsequently adjusted. See, Case No. GM-94-252, Report and Order dated October 12, 1994.

The 1989 and 1994 orders contain language requiring physical separation of MPC's intrastate pipeline from the TMP. In light of issues raised during this case, Gateway is requesting clarification of this language.

The 1989 order requires: "the physical separation of the intrastate pipeline from the portion of the Applicant's segment crossing the state boundary into Illinois."

The 1994 order states: "As to the physical separation of MPC's intrastate pipeline from a portion of a pipeline which crosses the Mississippi River, all parties agree the prohibitions against connecting the intrastate system to the interstate system is a condition which was imposed at the time the certificate was issued to MPC in Case No. GA-80-126, and that it will remain a condition of the certificate if transferred."

The certificate restriction in the 1989 order, particularly in light of the reference in 1994, shows that this restriction is intended to assure the state jurisdictional status of MPC. The greatest assurance to preventing FERC jurisdiction is to maintain a physical separation of MPC and the TMP. However, doing so simply to prevent a loss of state jurisdiction could preclude a significant opportunity to improve the profitability of MPC and MGC with minimal negative effects on consumers. An additional interconnection to bring gas into the state also presents benefits of lower cost gas services through competition and greater service reliability.

If TMP becomes operational, it will be held in a different company that would be under FERC jurisdiction and pursuant to Gateway's concession, an interconnection with MPC can be restricted to flow gas only into Missouri. With the conditions that the TMP be held in a corporation separate from MPC and that gas flow be restricted so that under an

interconnection of MPC and TMP gas will flow only into Missouri, the Commission finds that the 1989 certificate restriction can be modified to allow interconnection.

Conditions:

This Report and Order has previously addressed certain conditions. Staff's safety-related conditions were not contested and will be adopted. The findings in this case will not affect or apply to any subsequent ratemaking proceeding. Gateway has voluntarily offered conditions related to assuring continued state jurisdictional status for MPC and MGC and these will be adopted.

Laclede offered a list of seven conditions. The first proposed condition suggests a rate cap for a period of five years and a prohibition on rate restructuring. This condition relates to matters of private contract or matters best addressed in a tariff filing. Therefore, this condition is rejected.

Laclede's second condition suggests a rate freeze associated with lost volumes or increased expenditures. These are matters of private contract or matters best left for a tariff filing. Therefore, this condition is rejected.

Laclede's third condition is that MPC and MGC certificates should continue to forbid bypass. It is not necessary to order a condition that presently exists.

Laclede's fourth condition is that MPC and MGC should be required to provide existing users a right of first refusal for firm transportation. This is a matter that can be left to contract.

Laclede's fifth condition is that MPC and MGC should be prohibited from taking any actions that would subject them to FERC jurisdiction. The Commission has previously addressed this condition.

Laclede's sixth condition would require MPC and MGC to submit documentation showing that any plan to add firm transportation customers increasing peak throughput will not increase costs or lessen service reliability. This request presents an imposition on MPC and MGC that is burdensome and unnecessary absent a bad track record in Missouri. Such a condition is not warranted at this time.

Laclede withdrew its seventh condition.

Staff proposed seventeen conditions in its brief as Attachment A. Proposed conditions 1, 9, 16 and 18 all relate to issues that would arise in a rate case. The Commission will not prejudge these matters. Nothing in this Report and Order should be considered a finding regarding ratemaking treatment for any matter presented in this case or arising in the future.

Staff conditions 4, 5, 7 and 8 all relate to issues that would arise in a case presenting a stock or debt issuance or the creation of a lien on the property of a public utility. This Report and Order does not address or authorize any stock or debt issuance or any lien on the property of a public utility.

Staff condition 2 relates to the interconnection of the MPC pipeline system with the TMP and the current restriction that the MPC system be physically separated from the TMP. The Commission is conditionally waiving this certificate restriction.

Staff condition 3 requests continuance of "bypass" restrictions. The certificates of MPC and MGC presently prohibit bypass of local distribution systems and these restrictions are not affected by this Report and Order.

Staff condition 13 requires Gateway to comply with the Commission's affiliate transaction rule. This Report and Order does not waive or alter the application of the Commission's affiliate transaction rule.

Staff condition 14 would require Gateway to file tariffs. Gateway is not a public utility company. The tariffs of MGC and MPC are not affected or changed in this case.

Staff conditions 10, 11, and 12 relate to safety conditions agreed and accepted by the applicants and these will be adopted.

Staff conditions 6, 15 and 17 relate to the obligation of Gateway, MPC and MGC to report certain information to the Commission's Staff regarding the completion of the Stock Purchase Agreement, compliance with conditions and financial and service performance of MPC and MGC or their affiliates. The Commission has complete investigative powers to obtain information necessary to carry out its duties. The Commission will require certain information to be reported regarding the matters presented in this case. However, the Commission, the Staff and the Office of Public Counsel are not precluded from requesting and obtaining additional information in the future.

The Commission finds that it will require, as a condition of approval, that Gateway cooperate fully with the Commission's Staff to keep it informed of its financial status and performance. In this regard the Commission will require Gateway to provide the Commission's Staff with all final financing and equity investment agreements with pricing and contribution amounts in regard to Gateway's acquisition of UPL's stock. Further, Gateway shall provide the Commission's Staff with all reports and notices filed with Banc One or any successor lender for a period of five years and shall provide the Commission's

Staff with documentation for any short-term or long-term financing undertaken to replace the credit facility provided by Banc One.

The Commission also finds that if the transaction is closed during the period of November 1, 2001, to March 31, 2002, that Gateway and UtiliCorp shall enter a Transitional Services Agreement for Gateway to retain the services of UtiliCorp employees for the administration of nominations during the 2001-2002 winter heating season.

Amicus Brief:

On September 18, 2001, the Municipal Gas Commission of Missouri (MGCM) for itself and on behalf of the cities of Cuba, Richland, St. James, Sullivan, and Waynesville, Missouri and for Fidelity Natural Gas, Inc., filed a joint request to file a brief as amicus curiae and filed their amicus brief.

The request states a reasonable basis in support of the interests of these entities in this case. No party opposed the filing of this amicus brief. The brief will be accepted.

The amicus brief addressed the issues presented in this case and opposed approval of the Stock Purchase Agreement presenting the same grounds and arguments as presented by other parties. This Report and Order addresses the issues and arguments presented in the amicus brief.

Pending Motions Disposed:

In its brief, Staff raised a procedural issue that UtiliCorp was not a party to the application filed in this case and that the application did not satisfy the requirements of an application to sell or otherwise dispose of property. Staff did not file a motion to dismiss. Nevertheless, UtiliCorp responded with a Motion to Strike and Staff filed a reply.

Staff's argument is not persuasive. The Commission recognized that UtiliCorp was a necessary party and joined UtiliCorp in an order issued on May 24, 2001. Furthermore, the Commission ordered UtiliCorp to file a tax impact statement as required under Section 393.190.1, RSMo 2000, and in an application for authority to sell, transfer or assign assets under 4CSR 240-2.060(7). UtiliCorp complied.

UtiliCorp was joined as a party and was not an applicant for purposes of the applicant filing information required under 4 CSR 240-2.060(1). However, this information has been presented to the Commission in previous applications filed by UtiliCorp. The remaining information required under this rule is not material to the issues presented in this case. There is no material or substantive deficiency in the application or status of this case to warrant a dismissal.

All remaining motions not specifically addressed or otherwise disposed in this Report and Order are denied.

Conclusions of Law

The Missouri Public Service Commission has jurisdiction over the parties and the subject matter of this case pursuant to Section 393.190, RSMo 2000.

The Missouri Supreme Court stated the Commission's duty and the interests to be balanced in transactions as presented in this case in *State ex. Rel City of St. Louis v. Public Service Commission*, 73 S.W.2d 393 (Mo. 1934).

To prevent injury to the public, in the clashing of private interest with public good in the operation of public utilities, is one of the most important functions of public service commissions. It is not their province to insist that the public shall be benefited, as a condition to change of ownership, but their duty is to see that no such change

shall be made as would work to the public detriment. "In the public interest", in such cases, can reasonably mean no more than "not detrimental to the public."

Id. at 400.

The owners of this stock should have something to say as to whether they can sell it or not. To deny them that right would be to deny them an incident important to ownership of property ... a property owner should be allowed to sell his property unless it would be detrimental to the public.

Id.

The Commission applies this standard in transactions presented under Section 393.190, RSMo, and pursuant to Commission Rule 4 CSR 240-2.060(7) / (12), the Applicants must show why the proposed transaction is not detrimental to the public interest.

"The obvious purpose of [Section 393.190] is to ensure the continuation of adequate service to the public served by the utility." *State ex rel. Fee Fee Trunk Sewer, Inc. v. Litz*, 596 S.W.2d 466, 468 (Mo. App., E.D. 1980). To that end, the Commission has previously considered such factors as the applicant's experience in the utility industry; the applicant's history of service difficulties; the applicant's general financial health and ability to absorb the proposed transaction; and the applicant's ability to operate the asset safely and efficiently. See *In the Matter of the Joint Application of Missouri Gas Energy et al.*, Case No. GM-94-252 (*Report and Order*, issued October 12, 1994) 3 Mo.P.S.C.3d 216, 220.

The Commission concludes that the transaction presented in this case should be approved because after considering all the evidence presented Gateway and UtiliCorp have shown that completion and closing of their Stock Purchase Agreement is not

detrimental to the public interest. The issues of detriment presented by the parties in opposition are not sufficient to present a detriment to the public, or are offset by benefits or are mitigated by the conditions approved by the Commission.

Decision

The application authorizing Gateway Pipeline Company to buy all the shares of UtiliCorp Pipeline Systems under a Stock Purchase Agreement with UtiliCorp United Inc. is approved subject to the conditions of this Report and Order.

IT IS THEREFORE ORDERED:

1. That the application authorizing Gateway Pipeline Company, Inc. to buy all the shares of UtiliCorp Pipeline Systems under a Stock Purchase Agreement with UtiliCorp United Inc. is approved subject to the conditions of this Report and Order

2. That nothing in this order shall be considered a finding by the Commission of the value for ratemaking purposes of the transaction presented. The Commission reserves the right to consider any ratemaking treatment to be afforded the transactions herein involved in a later proceeding.

3. That Missouri Pipeline Company and Missouri Gas Company shall follow the pipeline safety regulations as contained in 4 CSR 240-40.020, 40.030, and 40.080.

4. That Missouri Pipeline Company and Missouri Gas Company shall continue to use an adequate number of qualified personnel to operate and maintain the pipelines and respond to any emergencies along the pipeline and that these personnel must continue to be qualified in accordance with 4 CSR 240-40.030(12)(D).

5. That there shall be no lapse in the call center, dispatch, emergency response, the Supervisory Control and Data Acquisition (SCADA) system, and gas control functions for Missouri Pipeline Company and Missouri Gas Company during the transition of ownership.

6. That Gateway Pipeline Company, Inc., Missouri Pipeline Company and Missouri Gas Company shall cooperate fully with the Commission's Staff to keep the Commission informed of their financial status and performance. In this regard the Commission will require Gateway Pipeline Company, Inc. and its affiliates to provide the Commission's Staff with all final financing and equity investment agreements with pricing and contribution amounts in regard to Gateway Pipeline Company, Inc.'s acquisition of UtiliCorp Pipeline Systems' stock. Further, Gateway Pipeline Company, Inc. and its affiliates shall provide the Commission's Staff with all reports and notices filed with Banc One or any successor lender for a period of five years and shall provide the Commission's Staff with documentation for any short-term or long-term financing undertaken to replace the credit facility provided by Banc One.

7. That if the stock purchase transaction is closed during the period of November 1, 2001, to March 31, 2002, that UtiliCorp United Inc. and Gateway Pipeline Company, Inc. with its affiliates shall enter a Transitional Services Agreement for Gateway Pipeline Company, Inc. or its affiliates to retain the services of UtiliCorp United Inc. employees for the administration of nominations for Missouri Pipeline Company and Missouri Gas Company during the 2001-2002 winter heating season.

8. That if Gateway Pipeline Company, Inc. causes the Trans Mississippi Pipeline to become operational it will be held in a company separate from Missouri

Pipeline Company and from Missouri Gas Company and that any interconnection with the system of Missouri Pipeline Company shall be restricted to flow gas only into Missouri in order to assure continued state jurisdiction under the Hinshaw exemption. So long as these conditions are met the restriction in Missouri Pipeline Company's certificate of authority issued in 1989 shall be waived to allow interconnection.

9. That all motions not previously ruled upon by the Commission in this case are denied, all objections not previously ruled upon are overruled, and all evidence the admission of which was not specifically denied is admitted.

10. This Report and Order shall become effective on October 18, 2001.

BY THE COMMISSION

A handwritten signature in black ink that reads "Dale Hardy Roberts". The signature is written in a cursive, flowing style.

**Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge**

(S E A L)

Simmons, Ch., Murray, Lumpe,
and Gaw, CC., concur; and certify
compliance with the provisions of
Section 536.080, RSMo 2000.

Dated at Jefferson City, Missouri,
on this 9th day of October, 2001.

4-0 A A

AL/Secretary:

Thornburg, Joyce

10-4

Date Circulated

CM-2001-585
CASE NO.

KS

Simmons, Chair

Nov 12 2001
Murray, Commissioner

Oct 8, 9, 17, 20, 22, 24, 25, 27/9
Lumpe, Commissioner

7/16/9
Gaw, Commissioner

Commissioner

Agenda Date

10-9

Action taken:

Must Vote Not Later Than

STATE OF MISSOURI

OFFICE OF THE PUBLIC SERVICE COMMISSION

I have compared the preceding copy with the original on file in this office and
I do hereby certify the same to be a true copy therefrom and the whole thereof.

WITNESS my hand and seal of the Public Service Commission, at Jefferson City,
Missouri, this 9th day of Oct. 2001.

Dale Hardy Roberts

Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge

