

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF DLR ENTERPRISES, INC.)	
AND COW CREEK GAS, INC. FOR APPROVAL)	CASE NO.
OF THE TRANSFER OF CERTAIN ASSETS)	2007-00419
FORMERLY OWNED AND CONTROLLED BY)	
SIGMA GAS CORPORATION)	

O R D E R

On September 25, 2007, DLR Enterprises, Inc. (“DLR”) and Cow Creek Gas, Inc. (“Cow Creek”) (collectively, “Joint Applicants”) filed an application, pursuant to KRS 278.020(5) and 278.020(6), requesting Commission approval to acquire the assets formerly owned and controlled by Sigma Gas Corporation (“Sigma”). The Commission, having considered the record and being otherwise sufficiently advised, finds that, with the Joint Applicants’ acceptance of certain conditions, the requested approval should be granted.

PROCEDURE

On October 3, 2007, the Commission granted the Joint Applicants’ motion to incorporate, by reference, the information filed by Jerome A. Kanney and Dennis L. Rohrer in Case No. 2005-00373¹ and established a procedural schedule that provided for two rounds of discovery.

¹ Case No. 2005-00073, Joint Application of Jerome A. Kanney and Dennis L. Rohrer for Authorization of the Acquisition of the Corporate Stock of Sigma Gas Corporation from Estill Branham, Barkley Sturgill, and Ruth Conley Clemmons.

PARTIES TO THE TRANSACTION

Sigma is a local gas distribution company² that serves approximately 558³ customers in the city of Salyersville (“Salyersville”) and surrounding areas in Magoffin County and is a utility subject to the Commission’s jurisdiction.⁴ It filed a voluntary petition for bankruptcy in the United States Bankruptcy Court for the Eastern District of Kentucky (“Bankruptcy Court”) under Chapter 7 of the Bankruptcy Code on October 20, 2004.⁵ The Bankruptcy Trustee abandoned all of the bankruptcy estate’s interest in the assets on or about October 27, 2004.

Salyersville is presently managing and operating Sigma pursuant to a management agreement entered into by Sigma, Salyersville, and the Governor’s Office of Local Development (“GOLD”), one of Sigma’s principal creditors, on July 6, 2005 and renewed on April 6, 2007. On July 23, 2007, the Bankruptcy Court approved an Agreed Order wherein Salyersville agreed to continue to operate Sigma until the transfer proposed herein has been completed or until further order of the Bankruptcy Court.

² Sigma Gas Corporation was incorporated in Kentucky on March 11, 1993, but was administratively dissolved on January 8, 2006. See Application, Exhibit 6.

³ Response to Commission Staff’s First Data Request, Item 3(a).

⁴ KRS 278.010(3)(b).

⁵ In Re: Sigma Gas Corporation, Case No. 04-71003, (Bankr. E.D. Ky., filed October 20, 2004).

DLR is a corporation organized under the laws of Kentucky and headquartered in Pikeville, Pike County, Kentucky. It is in good standing with the Office of the Kentucky Secretary of State.⁶

Cow Creek is a Kentucky corporation engaged in the distribution of natural gas to approximately 60 customers in Floyd County, Kentucky⁷ and is a utility subject to the jurisdiction of this Commission pursuant to KRS 278.010(3)(b). It also is in good standing with the Office of the Kentucky Secretary of State.⁸

OVERVIEW OF THE PROPOSED TRANSACTION

The Bankruptcy Court authorized the transfer of Sigma's assets to DLR, or its designee, pursuant to the terms and conditions of the Asset Purchase Agreements ("APAs") attached as Exhibit 9 to the application herein. Pursuant to the APAs, Sigma's assets are to be divided into two separate businesses. One business encompasses the gas operations located principally within the city limits of Salyersville as well as all end-use customer taps, whether inside or outside the city limits of Salyersville ("City Business"). The other business encompasses all the gas-gathering operations, excluding end-use customer taps, located principally outside the city limits of Salyersville ("Rural Business"). Since Sigma's assets are utility assets, the proposed transfer also requires this Commission's authorization.

⁶ See Kentucky Secretary of State Online Database, available at <http://apps.sos.ky.gov/business/obdb/showentity.aspx?id=0238347&ct=09&cs=99999>.

⁷ Annual Report of Cow Creek Gas, Inc. to the Public Service Commission of Kentucky for the year ended December 31, 2007 at 9.

⁸ See Kentucky Secretary of State Online Database, available at <http://apps.sos.ky.gov/business/obdb/showentity.aspx?id=0307731&ct=09&cs=99999>

The Joint Applicants request that the Commission approve the APAs and that it authorize the transfer of the City Business to Cow Creek and the Rural Business to DLR. Under the terms of the APAs, both businesses will be transferred to DLR or its designee. DLR has designated its affiliate, Cow Creek, to acquire the City Business pursuant to the terms of the APA.⁹ If the transfer is approved, Cow Creek agrees to continue providing service to Sigma's customers under the current terms and conditions and to adopt Sigma's tariffs and file an adoption notice to that effect, pursuant to 807 KAR 5:011, Section 11. It states, however, that once the City Business is merged with its present distribution operations, it will begin preparing a new rate application to reflect its actual cost to serve its combined system.

Pursuant to the Bankruptcy Court order and the APAs, DLR will pay GOLD \$750,000 for its secured interest as a result of loans made to Sigma and will pay certain administrative expenses which are estimated to be no more than \$100,000. The initial funding for the transaction will be provided by two 1-year, 9 percent loans from the owners, Jerome Kanney and Dennis L. Rohrer, to DLR and Cow Creek in the approximate amount of \$425,000 each.¹⁰

STATUTORY STANDARD

Under KRS 278.020(5), no person may acquire or transfer control of a utility until the Commission has determined that the acquirer has the financial, technical, and managerial abilities to provide reasonable service. In addition, under KRS 278.020(6),

⁹ Response to Commission Staff's Second Data Request, Item 8.

¹⁰ The actual amount is dependent upon the amount of administrative expenses due at the time of closing. See Response to Commission Staff's First Data Request, Item 7(a).

no individual may acquire control of a utility unless the Commission has determined that the acquisition is made in accordance with the law, for a proper purpose, and is consistent with the public interest.

DISCUSSION

Financial, Technical, and Managerial Ability Standard

Joint Applicants state that they have the financial, technical, and managerial abilities to provide utility service to Sigma's customers and thus meet the requirements of KRS 278.020(5). They assert that Mr. Kanney and Mr. Rohrer are hands-on managers who have previously been deemed by this Commission to have the requisite abilities to operate a gas utility system in this Commonwealth.¹¹ In addition to Mr. Kanney and Mr. Rohrer, the Joint Applicants provided a list of employees who will be responsible for the day-to-day operations of the utility system and a summary of their experience and qualification.

The Joint Applicants have explained that they are familiar with the Uniform System of Accounts ("USoA") adopted by the Commission for natural gas utilities and the Commission's annual regulatory accounting and reporting requirements¹² as they currently comply with these requirements for Cow Creek and another jurisdictional regulated gas company, Dema Gas Co., Inc. ("Dema").¹³

¹¹ Application at 2.

¹² Response to Commission Staff's First Data Request, Item 1(a).

¹³ Dema is a natural gas utility that provides service to 12 customers in Knott County, Kentucky. See Annual Report of Dema Gas Co., Inc. to the Public Service Commission of Kentucky for calendar year ended December 31, 2006.

The Joint Applicants have also provided information to support their claim that they will have the financial ability to provide reasonable service. In addition to the loans mentioned above from the owners, Cow Creek will have immediate access to a \$250,000 line of credit from Community Trust Bank.

Public Interest Standard

The Commission has previously held that a transfer is in the “public interest” if it does not adversely affect the existing level of utility service or rates or that any potentially adverse effects can be avoided through the Commission’s imposition of reasonable conditions on the acquiring party.

The Joint Applicants assert that the public interest standard is met. They state that management and operational service will be provided to Sigma, a troubled system, by experienced, competent management and that the uncertainty that has surrounded the utility during the bankruptcy will finally be resolved. The Joint Applicants note that the Commission placed reporting and monitoring conditions on the transfer approved for ALLTEL, Inc. in Case No. 2001-00399.¹⁴ While the Joint Applicants believe that they have provided sufficient evidence to prove that the proposed transfer is in the public interest, they do not object to similar reporting and monitoring conditions.

The Bankruptcy Court found that the “Debtor had only two options: (a) sell all of its assets, or (b) cease operations.”¹⁵ It further found that since Sigma is a utility providing gas service to several hundred customers, it was not in the best interest of the

¹⁴ Case No. 2001-00399, Petition by ALLTEL Corporation to Acquire the Kentucky Assets of Verizon South, Incorporated.

¹⁵ Application, Exhibit 1, at 7.

public to cease operations. While Salyersville previously expressed an interest in purchasing the Sigma system, DLR and Cow Creek are the only parties that are presently interested in acquiring the system.

FINDINGS

Having reviewed the record and being otherwise sufficiently advised, the Commission finds that, if the proposed APAs are approved, DLR will not be a utility as defined by KRS 278.010 as it will not be providing service to the public.¹⁶ Cow Creek, on the other hand, will be a utility as defined by the statute and will be subject to the Commission's jurisdiction.¹⁷

The Commission finds that the Joint Applicants have provided sufficient evidence to support their assertion that Cow Creek will have the financial, technical, and managerial ability to provide reasonable service to Sigma's customers. The Commission further finds that the proposed transfer is in accordance with the law and for a proper purpose. However, due to the circumstances of Sigma's bankruptcy, several years have elapsed since the Commission has received annual reports and several months have elapsed since we have received gas cost adjustment ("GCA") filings for Sigma. As a result, the proposed acquisition will be in the public interest only if the Joint Applicants agree to the following conditions:

1. Adoption of Sigma's rates, etc., means adopting Sigma's GCA clause. The GCA clause requires quarterly filings based on the utility's current wholesale cost of gas. Cow Creek is required to submit a GCA filing within 30 days from the date of this Order, based on the current cost of gas to serve its newly acquired customers, with an effective date not later than February 1, 2008.

¹⁶ DLR could become subject to limited Commission jurisdiction if it were to provide service to farm-tap customers pursuant to KRS 278.470.

2. The most recent Sigma annual report filed with the Commission covered calendar year 2004. Based on the information contained in that report, plus the detailed depreciation schedule contained in Exhibit 1 of Joint Applicants' response to the Commission Staff's supplemental data request, Cow Creek is to update the accumulated depreciation balance recorded on the assets which it is acquiring for the period from December 31, 2004 up to the date of closing on the asset acquisition. This update is to be filed within 60 days from the date of this Order.
3. Joint Applicants are required to file a schedule of the assets being acquired, their net book value as of the date of closing (based on the depreciation update discussed previously), which shows separately, the original cost, accumulated depreciation, and net book value of the assets acquired by Cow Creek and the original cost, accumulated depreciation, and net book value of the assets acquired by DLR. This schedule is to be filed within 60 days from the date of this Order.
4. Cow Creek is to file, within 7 business days from the date of this Order, a written response indicating whether or not it accepts the conditions enumerated herein and, in the event it accepts the conditions, an adoption notice in the form prescribed in 807 KAR 5:011, Section 15.

In addition to the above conditions, which are specific to this transfer, Joint Applicants are hereby notified that they are also required to file with the Commission the following information related to the asset acquisition:

1. In the event the closing of the proposed asset acquisition occurs before the end of calendar year 2007, Cow Creek will be required to file partial year financial data for the Sigma system for the portion of 2007 in which it owned the assets being acquired. This data should be included in Cow Creek's 2007 annual report to the Commission along with related workpapers and a narrative description regarding the Sigma data.
2. The accounting entries on Cow Creek's books to record its acquisition of the "City Business" portion of the Sigma assets are to be filed within 60 days from the date of this Order. These entries should be in accordance with the USoA for gas utilities adopted by the Commission.

IT IS THEREFORE ORDERED that:

1. The transfer of Sigma's assets to DLR and Cow Creek as proposed in the APAs is approved subject to Cow Creek's acceptance of the conditions set forth in this Order.

2. The proposed transfer shall not proceed unless, within 7 business days of the date of this Order, a written acknowledgement on behalf of Cow Creek by its chief executive officer accepting and agreeing to be bound by the conditions is filed with the Commission. If the conditions are accepted, Cow Creek shall file an adoption notice pursuant to 807 KAR 5:011, Section 11, and in the form prescribed in 807 KAR 5:011, Section 15.

3. Within 5 days of the consummation of the proposed transaction, the Joint Applicants shall file a written notice setting forth the date of the acquisition.

4. The financial and accounting data identified in the Findings portion of this Order shall be filed with the Commission within the time periods stated therein.

Done at Frankfort, Kentucky, this 21st day of November, 2007.

By the Commission

Commissioner Clark Abstains.

ATTEST:



Executive Director