

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

SIGMA GAS CORPORATION)	
)	
COMPLAINANT)	
V.)	CASE NO. 2004-00018
)	
B.T.U. GAS COMPANY, INC.)	
)	
DEFENDANT)	

O R D E R

On January 14, 2004, Sigma Gas Corporation (“Sigma”) filed a complaint alleging that B.T.U. Gas Company, Inc. (“BTU”) had extended its gas facilities in and around the city of Salyersville, Kentucky by connecting a number of customers that Sigma could serve. Sigma also complains that BTU is now serving customers that were previously served by Sigma. Sigma alleges that BTU is in violation of KRS 278.020 for failure to obtain a Certificate of Public Convenience and Necessity (“CPCN”) from the Commission prior to construction of those facilities. Both Sigma and BTU were jurisdictional Local Distribution Companies (“LDCs”) at the time.¹

¹ KRS 278.504(3) defines Local Distribution Company (“LDC”) as: “Local distribution company” means any utility or any other person, other than an interstate pipeline or an intrastate pipeline, engaged in transportation or local distribution of natural gas and the sale of natural gas for ultimate consumption, but shall not include any part of any pipeline primarily used for storage or gathering or low pressure distribution of natural gas.

On March 17, 2008, the Commission entered an Order to determine if this case should remain on the Commission's docket or be dismissed. In that Order, the Commission found that Sigma had been administratively dissolved and its assets had been transferred to DLR Enterprises, Inc. ("DLR") and Cow Creek Gas, Inc. ("Cow Creek"). Due to this transfer, the Commission, by Order, afforded DLR and Cow Creek an opportunity to request intervention in this matter to demonstrate why the Commission should proceed to issue a decision on the merits of the original complaint and for all parties to show cause why the proceedings should not be dismissed. Cow Creek was the only entity filing a response to that Order. The Commission granted the motion of Cow Creek for full intervention and ruled that Cow Creek stood in the shoes of Sigma² and, as such, assumed the existing record.

ANALYSIS AND DISCUSSION

First, we will determine the initial issue on the merits as to whether BTU was required to obtain a CPCN prior to constructing any facilities to provide service to the areas in question. Second, we will then determine what relief, if any, can be afforded to Cow Creek as the party acquiring the assets of Sigma.

Both parties have filed briefs in the case. Sigma, in its brief, maintains that this case is similar to the Cooper Tire³ case in which Columbia Gas of Kentucky, Inc. ("Columbia"), at the request of a customer, applied for a CPCN to construct facilities to

² We will continue to refer to Sigma in this matter rather than replace the name Sigma with Cow Creek.

³ Case No. 1996-00015, Application of Columbia Gas of Kentucky, Inc. for an Order Issuing a Certificate of Public Convenience and Necessity to the Extent Such a Certificate Is Required to Construct a Pipeline to Service Cooper Tire, Inc. in Mt. Sterling, Kentucky (Ky. PSC Jul. 10, 1996).

serve that customer in an area being served by Delta Gas Company, Inc. ("Delta"). Sigma cites to the holding of that case in which the Commission held that the proposal to construct facilities was not in the ordinary extension of service, since such construction would conflict with the existing Delta service. Sigma also points to the issue of duplication of existing facilities caused by BTU's extension of service. Sigma argues that, because there is a duplication of existing facilities, it is a wasteful duplication. Sigma stresses that there is no evidence of any inadequacy of existing service or unwillingness on the part of Sigma to render adequate service. Sigma does contend that there will be a "direct impact on Sigma" by the loss of customers to BTU. Sigma also claims that it was at all times ready, willing, and able to provide gas service to any current or potential customers. Sigma rebuts BTU's "customer choice" claim by reference to Administrative Case No. 297,⁴ where the Commission said that a utility proposing a physical bypass of an LDC in order to accommodate the use of natural gas by an end-user should be required to make an application to this Commission requesting a CPCN to bypass the LDC.

BTU, in its brief, argues that its plant extensions were in the ordinary course of business. BTU claims that the customers it began serving were in the general area of the BTU distribution system and that the cost to BTU was nominal. BTU states that Sigma does not have exclusive franchise rights to operate in Salyersville and that Sigma has "no right to a competition free service area." BTU further claims that the option to choose a gas supplier will benefit the customers and that BTU will supply

⁴ Administrative Case No. 297, An Investigation of the Impact of Federal Policy on Natural Gas to Kentucky Consumers and Suppliers (Ky. PSC May 29, 1987).

those customers with significantly lower rates than Sigma. BTU also claims that there is no evidence of wasteful duplication or conflict with existing services of other utilities.

While the Commission lacks authority to establish an exclusive service territory for local gas distribution utilities,⁵ the Commission clearly possesses the authority to consider competing utilities' claims to provide service to a prospective customer to prevent wasteful duplication of facilities or excessive investment.⁶

KRS 278.020(1) limits the construction or service that a utility may undertake without obtaining prior Commission approval.

No person, partnership, public or private corporation, or combination thereof shall commence providing utility service to or for the public or begin the construction of any plant, equipment, property, or facility for furnishing to the public any of the services enumerated in KRS 278.010, except retail electric suppliers for service connections to electric consuming facilities located within its certified territory and ordinary extensions of existing systems in the usual course of business, until that person has obtained from the Public Service Commission a certificate that public convenience and necessity require the service or construction.

⁵ Controversies between persons or corporate bodies engaged in a public utility enterprise concerning the right to construct new facilities to serve a particular customer or class of customers (other than ordinary extensions of existing systems in the usual course of business) are within the jurisdiction of the Public Service Commission upon application made under KRS 278.020 for a certificate of public convenience and necessity. *City of Cold Spring v. Campbell County Water*, 334 S.W.2d 269, 274 (Ky. 1960) overruled on other grounds by *City of Georgetown v. Pub. Ser. Comm'n*, 516 S.W.2d 842 (Ky. 1974) (holding that KRS 278.020 is not applicable to cities and does not require a city to obtain a certificate of public convenience and necessity).

⁶ See *Kentucky Utilities Co. v. Pub. Sew. Comm'n*, 390 S.W.2d 168, 175 (Ky. 1965). See, e.g., Case No. 1991-00359, Application of Kentucky-American Water Company for a Certificate of Public Convenience and Necessity Authorizing the Construction of Approximately 49,000 Feet of 24" Main, 400 Feet of 12" Main, 240 Feet of 8" Main with Associated Valves and Fittings, Known as the "Jack's Creek Pipeline" (Ky. PSC Apr. 17, 1992) at 4; Case No. 1991-00316, Mountain Utilities, Inc. v Equitable Gas Co. (Ky. PSC Apr. 6, 1992) at 3.

While exempting “ordinary extensions” from the requirement for Commission approval, the General Assembly did not define “ordinary extensions.” To define “ordinary extensions,” the Commission promulgated 807 KAR 5:001, Section 9(3), which provides:

Extensions in the ordinary course of business.

No certificate of public convenience and necessity will be required for extensions that do not create wasteful duplication of plant, equipment, property or facilities, or conflict with the existing certificates or service of other utilities operating in the same area and under the jurisdiction of the commission that are in the general area in which the utility renders service or contiguous thereto, and that do not involve sufficient capital outlay to materially affect the existing financial condition of the utility involved, or will not result in increased charges to its customers.

Since KRS 278.020(1) provides a clear mandate that a utility must apply for and obtain a CPCN prior to providing service or construction of utility plant, we must determine if there is any exception from that requirement. 807 KAR 5:001, Section 9(3), provides certain essential elements for obtaining that exemption which is intended to allow regulated utilities the freedom of proceeding with relatively minor construction work required in the ordinary course of business without obtaining commission approval for such work.⁷

EXTENSION IN THE ORDINARY COURSE

If a utility’s plant or service does not meet the exception as provided in 807 KAR 5:001, Section 9(3), then it does not qualify for the exemption from obtaining a CPCN. If it does qualify for the exemption, then no CPCN will be required.

⁷ *Id.* Case No. 1991-00316 (Ky. PSC Apr. 6, 1992) at 5.

BTU admits it has constructed facilities in Salyersville. There is no evidence in the record of BTU having obtained a CPCN to construct those facilities within the area being served by Sigma.⁸ This fact alone disqualifies BTU from the exception provided in 807 KAR 5:001, Section 9.

If a conflict or potential conflict exists, it is up to the Commission to decide the issue of which utility may serve, and that can only be resolved in a hearing before the Commission, not by the unilateral action of a utility.

When two LDCs have facilities near each other, the utility seeking to extend service must show an element of lack of adequate capacity to serve, primarily by the nearer or more available LDC. The holding in *Cooper Tire*⁹ requires a showing of “substantial inadequacy of existing service” due to “substantial deficiency of service facilities” or to “indifference, poor management or disregard for the rights of consumers” so as to establish over time an inability or unwillingness to render adequate service. These are factors the Commission is required to consider if a proper application for such a determination is presented to it. The record in this case clearly demonstrates that BTU did not apply for such a determination but acted unilaterally without seeking Commission approval.

SERVICE AREA

The Commission also referred to “service areas” in Administrative Case No. 297:¹⁰

⁸ Transcript of Evidence of Formal Hearing of June 29, 2004 (“T.E.”) at 71.

⁹ *Id.* at 4.

¹⁰ Administrative Case No. 297 (Ky. PSC May 29, 1987) at 55-56.

The Commission finds it undesirable to designate a precise geographical area for each utility's service area. Although the Commission will not establish maps for natural gas service areas, any user of natural gas is assumed to be a customer of the distribution company serving other residential, commercial, and industrial customers in the vicinity. Likewise, any new customer would become a customer of the LDC. This will allow the LDC first opportunity to serve customers and promote use of the LDC's facilities, yet the territories will remain open to provide access to competition.

There is a presumption that an LDC has the ability to serve any customer who may locate or be located within proximity to its existing facilities. However, the ultimate decision of whether the LDC or a competing utility will provide the service remains with the Commission. This practice differs neither from current practice nor from what might occur if service areas were established. The Commission intends for the existing distribution facilities to be used optimally. If there is a void in the system which can be remedied most efficiently by the construction of facilities by someone other than the LDC, it should be allowed. This policy merely recognizes that the LDC, generally, has the facilities in place that can be used economically to meet normal growth and demand for gas within a given locale.

The new service connections by BTU are contrary to established policy and law. There is no evidence in the record that Sigma was unwilling or unable to serve the customers or areas in issue. Estill Branham, President and Manager of Sigma,¹¹ testified that, as to the new Magoffin County Courthouse, Sigma had a two-inch riser at the location prior to the courthouse construction and had to cap off and remove some of that line to be out of the way during construction.¹² Mr. Branham further testified that

¹¹ T.E. at 12.

¹² T.E. at 17-18.

the Magoffin County Teen Coalition was being served by Sigma but that the Teen Coalition directed Sigma to remove its meter, which was then replaced by a meter set by BTU.¹³ Mr. Branham further testified that, in the “Dixie” area of Salyersville, Sigma had experienced loss of customer base due to switching service to BTU.¹⁴ We gather from the evidence that the “Dixie” area is served by both LDCs, that the service appears to have been undertaken based upon prior mutual agreement between the parties as a result of the division or dismemberment of the old Salyersville Gas Company system, and that the customers served by BTU as farm tap customers were then incorporated into the BTU distribution system.¹⁵

Mr. Branham also testified that Sigma had facilities throughout the area and was capable of serving any customer within that area. He further testified that Sigma borrowed \$1.3 million to construct a 20- and a 10-inch line; that Sigma will not have enough revenue to pay bills and keep the company going if it loses those customers¹⁶; that, if Sigma continues to lose customers, Sigma facilities will be overbuilt; and that Sigma would have excess capacity due to the increased line constructed to handle the anticipated load.¹⁷ Referring to the Sigma service area, Mr. Branham testified that Sigma, after its acquisition of a portion of the old Salyersville Gas Company, began service to the College Street Teen Scene Area in 1994.

¹³ T.E. at 18-19.

¹⁴ T.E. at 20-21.

¹⁵ T.E. at 87-89.

¹⁶ T.E. at 22.

¹⁷ T.E. at 22-23.

Richard D. Williams, Operations Manager of BTU, testified in Case No. 1992-00220¹⁸ concerning the bankruptcy of Salyersville Gas Company and when BTU became a Public Service Commission company.¹⁹ We will look at three of the listed customers that represent a cross-section of the customer issue groups: the “new” service; the “switched” service; and the “exchange” service.

First is the “new” service represented by the new Magoffin County Courthouse. Mr. Williams testified that BTU is serving the new Magoffin County Courthouse upon the request of the county judge.²⁰ Mr. Williams testified that the request was due to the difference in rates²¹ and the special arrangements for billing to be provided by BTU.²² In order to provide this service, BTU constructed 1,500 feet of new plant at a cost of

¹⁸ Case No. 1992-00220, Investigation of Richard Williams, d/b/a B.T.U. Pipeline, Inc., and M5-A1, Inc. On May 29, 1992, the Commission established this proceeding to determine the jurisdictional status of the R. C. Energy pipeline, to investigate certain rate and other issues related to a proposed tariff filed by BTU, and to determine the impact on Sigma and certain customers of serving the R. C. Energy pipeline from the Sigma distribution system (as proposed by M5-A1, Inc.). BTU had filed with the Commission a tariff pursuant to KRS 278.485 for a system commonly known as a farm tap system. The Commission determined that it was necessary to determine the jurisdictional status of the BTU facilities. As part of that investigation, Commission Staff inspected the BTU facilities and issued an inspection report which recommended that BTU facilities should be declared a gas distribution utility pursuant to KRS 278.010(3)(b). At a hearing held in that case, BTU accepted Commission Staff’s report as accurate and acknowledged BTU was a gas distribution company.

¹⁹ T.E. at 55-59.

²⁰ BTU Response to Commission Order filed March 29, 2004, Exhibit #4, Letter dated March 23, 2004 from County Judge/Executive Bill W. May.

²¹ T.E. at 62-63. Mr. Williams stated that the county judge placed the Sigma rate at \$16.40 and that the BTU rate was \$6.02.

²² The payment for this service was to be periodic or every 90 days for the gas service. BTU’s filed tariff states gas service is billed monthly, with all bills payable by the 10th of each month.

\$2,205, paid from BTU's reserve funds.²³ Also included in this group is the Teen Scene,²⁴ which BTU did not begin serving in that area until approximately 2000.²⁵ Mr. Williams testified that BTU constructed 500 feet of pipe to serve Teen Scene at a cost of \$300 and that he and his wife are paying for the gas furnished.²⁶

The "switched" service is represented by Burke Arnett, who switched from Sigma to BTU due to the difference in rates.²⁷

Third is the "exchange" service. It appears that BTU provides this type of service in exchange for either a right of way or lease agreement with the customer. Mr. Williams testified that the service to H. C. Prater was accomplished by construction of 200 feet of pipeline to serve him in exchange for a lease on Mr. Prater's property for a gas well.²⁸ However, the Prater lease is a considerable distance from the point of service and is not shown on the Reference Map.²⁹ The evidence shows that, in the construction for a new pipeline, BTU, in exchange for a right of way, constructed a "free

²³ T.E. at 63.

²⁴ The Teen Scene and the Magoffin County Teen coalition building appear to be one and the same.

²⁵ T.E. at 41-42.

²⁶ T.E. at 66-67.

²⁷ T.E. at 82.

²⁸ T. E. at 68.

²⁹ T.E. at 8-9, 94-95. The Reference Map is Staff Exhibit 1, a map dated June 22, 2004, prepared by Commission Staff to represent the two gas systems as stipulated at the formal hearing held on June 29, 2004.

tap” for a radio station and agreed to provide “free gas” for a right of way across Tommy Bailey’s property.³⁰

As is evident from the Reference Map, BTU constructed its pipe over, under, and beside that of Sigma in order to serve its new, switched, and exchange customers.³¹ Mr. Williams further testified that BTU knew that Sigma was already serving in the general area.³²

From the evidence, it can only be concluded that BTU believes that it is some sort of hybrid gas company, either an LDC, a gathering company, or a production company. However, that question was answered in Case No. 1992-00220,³³ wherein BTU was found to be an LDC governed by the provisions of KRS 278 and 807 KAR 5.

It also appears that BTU believes it can serve customers whenever and wherever it-wants to, regardless of whether a customer is presently being served by another LDC. That issue was discussed by the Commission in Administrative Case No. 297:

The ultimate decision on whether the LDC or a competing utility will provide the service remains with the Commission. This practice does not differ from current practice, nor does it differ from what might occur if service areas were established. The Commission intends for the existing distribution facilities to be used optimally. If there is a void in the system which can be remedied most efficiently by the construction of facilities by someone other than the LDC, it should be allowed. However, this policy merely recognizes that the LDC generally has the facilities in place that

³⁰ T.E. at 64-66.

³¹ T.E. at 91-92. See reference list of Dixie customers as contained in Response No. 2 of Response to Commission Order Dated April 6, 2004 as filed by BTU on April 13, 2004. See *also* the map filed by BTU in that same filing containing the BTU system in question along with pipeline sizes and customers.

³² T.E. at 73-74, 93.

³³ Case No. 1992-00220 (Ky. PSC Apr. 27, 1994).

can be used economically to meet normal growth and demand for gas within a given locale.³⁴

In Case No. 2003-00422,³⁵ the Commission was asked to prevent Columbia from extending service to a present customer of Natural Energy Utility Corp. (“NEUC”) without first obtaining a CPCN. The NEUC case was a matter of proposed service and construction. However, in this case, pipe is already in the ground and customers are being served.

In Case No.1996-00015,³⁶ NEUC filed a complaint against Columbia alleging that it was presently serving the customer to which Columbia was seeking to extend its service. Clearly, Columbia’s proposed construction was in conflict with NEUC’s existing service:

Having determined that Columbia’s proposed construction would conflict with NEUC’s present service to an existing customer, we need not address the further issue of wasteful duplication. We find sufficient evidence to demonstrate that the proposed construction is not an ordinary extension of an existing system in the usual course of business and that KRS 278.020(1) requires Columbia to obtain a Certificate prior to commencing such construction.

The Commission, *supra*, has determined that the extensions and service by BTU to the “new,” “switched,” and “exchange” customers are not, nor were they ever, in the ordinary course of its business. Since BTU’s actions are not exempt under 807 KAR 5:001, Section 9(3), BTU is required to first seek and obtain a CPCN prior to any such construction or service connections. Consequently, without a CPCN, any new customer

³⁴ Administrative Case No. 297 at 55-56.

³⁵ Case No. 2003-00422, Natural Energy Utility Corp. vs. Columbia Gas of Kentucky, Inc. (Ky. PSC Sept. 1, 2004).

³⁶ Case No. 1996-00015 (Ky. PSC Jul. 10, 1996).

BTU sought to serve in the area being served by Sigma would be presumed to be a customer of Sigma. Conversely, the opposite would be true if Sigma commenced to serve customers BTU had been serving in the area.

REMEDY

In the NEUC v. Columbia case,³⁷ the Commission ordered Columbia to refrain from any construction designed to provide gas service to NEUC's customers until it had obtained a CPCN for such service. Here, the Commission is presented with a *fait accompli* in that BTU has constructed facilities to serve and is presently serving customers. Therefore, the appropriate remedy would be to order BTU to cease service to those customers identified by Sigma in the complaint and by evidence taken at the hearing. In Case No. 10419,³⁸ Tranex Corp. constructed facilities and was serving a customer of Delta's without a CPCN to do so. Tranex was ordered to give notice to the customer and cease service. Likewise, in Case No 1991-00138,³⁹ Kentucky Ohio Gas, Inc. was ordered to cease service to a customer immediately for failure to obtain a CPCN. The present case is distinguished from the cited cases by the magnitude of the violations and number of customers served.

The choice of remedy to be applied here is further complicated by the intervening bankruptcy proceeding and the transfer to Cow Creek. After the parties filed briefs and the case was submitted to the Commission for a decision, Sigma filed a petition in

³⁷ Supra.

³⁸ Case No. 10419, Delta Natural Gas Co. vs. Tranex Corp. (Ky. PSC Jul. 16, 1990).

³⁹ Case No. 1991-00138, Columbia Gas of Kentucky, Inc. vs. Kentucky-Ohio Gas Co. (Ky. PSC Dec. 18, 1991).

bankruptcy.⁴⁰ Due to that filing, all further proceedings herein were suspended pending disposition of the bankruptcy matter. The bankruptcy resulted in the liquidation of Sigma and the acquirement of its assets by an enterprise which then applied to the Commission for approval of the transfer.⁴¹ The bankruptcy of Sigma and the transfer of Sigma's assets to Cow Creek raise questions as to how to apply a remedy for the violations of BTU. One of the many reasons for requiring a utility to seek a CPCN is that the offending utility's action could possibly result in another utility suffering such economic harm (loss of customers and revenue) as might result in bankruptcy. In this case, that possibility became fact.

BTU is not to provide any new service to any customer in the Salyersville area prior to obtaining a CPCN from the Commission to do so. As to those customers BTU commenced serving in the Salyersville area after January 1, 2000, a determination will have to be made as to whether or not Cow Creek is willing and financially able to reconnect to those customers and the time line in which those connections can be made. If Cow Creek is unable or unwilling to connect any customer on the list, then that customer may be served by BTU.

In its complaint, Sigma identified seven named and five unknown customers it claimed BTU had commenced serving without obtaining prior approval of the Commission in violation of KRS 278.020. This was further expanded by Sigma in its

⁴⁰ In Re: Sigma Gas Corporation, Case No. 04-71003, (Bankr. E.D. Ky. filed October 20, 2004).

⁴¹ Case No. 2007-00419, Application of DLR Enterprises, Inc. and Cow Creek Gas, Inc. for Approval of the Transfer of Certain Assets Formerly Owned and Controlled by Sigma Gas Company (Ky. PSC Nov. 21, 2007).

March 15, 2004 response to a Commission Order.⁴² In a March 29, 2004 response to the Commission Order of February 23, 2004, BTU filed a list of customers it serves in the area in question.⁴³ In comparing the two lists as filed, the following customers are admittedly served by BTU: Magoffin County Teen Coalition (Teen Scene); Magoffin County Courthouse; H. C. Prater; Burke Arnett; Tommy Howard; Magoffin County Recycling Center, and Tom Bailey's home and garage. (WRLV Radio station is listed as connected but not served.) It is these former or prospective customers of Sigma that have been connected by BTU since January 2000 without obtaining a CPCN to do so.⁴⁴

FINDINGS

1. KRS 278.020(1) requires any utility, prior to commencing providing service or any construction of facilities, to obtain a CPCN.
2. The exception to the requirement of obtaining a CPCN applies to that of ordinary extensions of existing systems in the usual course of business.
3. Sigma, at the time of the complaint, was ready, willing, and able to provide gas service to the customers it was serving
4. Sigma, at the time of the complaint, was ready, willing, and able to provide gas service to the potential new customers that are now served by BTU.
5. Cow Creek has acquired ownership of the assets of Sigma.

⁴² Sigma Response to Commission Order dated February 23, 2004, response to Item #1 and attachment.

⁴³ BTU Response to Commission Order dated February 23, 2004, response to Item #1a and attachment.

⁴⁴ BTU Response to Commission Order Filed March 29, 2004, Item #1a, Answer.

6. The transfer of ownership of the former distribution system of Sigma to Cow Creek has been approved by the Commission.

7. BTU's provision of service to the customers is not within the ordinary course of business.

8. BTU is in violation of KRS 278.020(1) by failing to obtain a CPCN for service to the customers previously being served by Sigma.

9. BTU is in violation of KRS 278.020(1) by failing to obtain a CPCN prior to connecting new customers in the area being served by Sigma.

10. BTU is not authorized to serve the customers previously served by Sigma in the "Dixie" area of Salyersville.

11. BTU is not authorized to serve the following customers in Salyersville: Magoffin County Teen Coalition (Teen Scene); Magoffin County Courthouse; H. C. Prater; Burke Arnett; Tommy Howard; Magoffin County Recycling Center; and Tom Bailey's home and garage. (WRLV Radio station is listed as connected but not served.)

12. BTU is not authorized to serve any new customer in the Salyersville area until it shall have been granted a CPCN to do so.

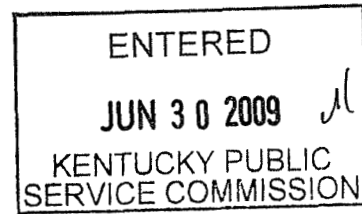
IT IS THEREFORE ORDERED that:

1. BTU is in violation of KRS 278.020(1) and is not authorized to serve customers of Sigma and any potential customer of Sigma in the Salyersville area.

2. Within 20 days of the date of this Order, BTU shall submit a list of those customers it still serves from those listed in findings #10 and #11 plus any additional customers it may have begun serving in the Salyersville area since June 29, 2004, the date of the hearing in this case.

3. Cow Creek shall notify the Commission in writing of its intention to serve those customers as contained in findings #10 and #11 and the time necessary to construct lines, set meters, and service lines to serve those customers.

By the Commission



ATTEST:



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