

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF KENTUCKY FRONTIER)
GAS, LLC FOR APPROVAL OF FINANCING AND) CASE NO. 2008-00394
TRANSFER OF CONTROL)

ORDER

Kentucky Frontier Gas, LLC ("Kentucky Frontier") has applied for authorization to issue evidences of indebtedness and to acquire control of six natural gas utilities. Finding that the statutory prerequisites have been met for the acquisition of three of the utilities in question, we authorize Kentucky Frontier's acquisition of those utilities, but deny the remaining portions of its application without prejudice.¹

PROCEDURE

On September 24, 2008, Kentucky Frontier applied for Commission authorization to issue evidences of indebtedness. It subsequently amended its application to request Commission authorization to acquire control of Belfry Gas, Inc. ("Belfry Gas"); Floyd County Gas; Elam Utility Company, Inc. ("Elam"); and Mike Little Gas Company ("Mike Little Gas") (collectively, "the Four Utilities"). It also sought authorization for the acquisition of control of B & H Gas Company, Inc. ("B & H") and Johnson County Gas, Inc. ("Johnson County").

¹ By Order of November 24, 2008, the Commission addressed that portion of Kentucky Frontier's application that requested authorization to issue evidences of indebtedness.

Elam is the only intervenor to this proceeding. It moved for intervention in this proceeding on October 16, 2008. We granted its motion on October 23, 2008.

On October 16, 2008, Commission Staff held an informal conference to discuss the proposed application with both parties to this proceeding. Following this conference, Commission Staff served document and information requests upon Kentucky Frontier. Kentucky Frontier has responded to those requests.

On November 21, 2008, Elam's legal counsel advised the Commission in writing of Elam's objection to its inclusion in Kentucky Frontier's application and to Kentucky Frontier's acquisition of its assets. Elam requested that the Commission remove any debt instruments that it has issued to the Department of Local Government ("GOLD")² from the agreement between Kentucky Frontier and GOLD for Kentucky Frontier's purchase of certain debt instruments from GOLD and that the Commission request GOLD to restructure Elam's existing debt arrangements.

On November 24, 2008, the Commission issued an Order dismissing that portion of Kentucky Frontier's application that requested Commission authorization to borrow \$1.7 million from Community Trust Bank, Inc. for lack of subject matter jurisdiction.

FINDINGS OF FACT

The Commission, based on the evidence of record and being otherwise sufficiently advised, finds that:

² The Kentucky Department of Local Government was previously known as the Governor's Office of Local Development. Its name was changed on June 16, 2008. See Executive Order 2008-509 (June 6, 2008). Because most of the documents in the record refer to the agency under its prior name, we have referred to the Department throughout this Order by its former acronym.

1. Belfry Gas, a Kentucky corporation owned in its entirety by J. W. Kinzer, owns and operates facilities that distribute and furnish natural gas to approximately 500 customers in eastern Pike County, Kentucky. Mr. Kinzer is the principal shareholder of Alert Oil & Gas Company, Inc. ("Alert Gas"), a Kentucky corporation that owns a natural gas gathering system that serves approximately 300 farm tap customers near Pikeville, Kentucky.

2. Floyd County owns and operates facilities that distribute and furnish natural gas to approximately 850 customers in Floyd County, Kentucky. Floyd County operates these facilities under the name "Floyd County Gas."

3. Elam, a Kentucky corporation, owns and operates facilities that distribute and furnish natural gas to approximately 430 customers in Morgan County, Kentucky.

4. Mike Little Gas, a Kentucky corporation, owns and operates facilities that distribute and furnish natural gas to approximately 350 customers in southwest Floyd County, Kentucky.

5. Kentucky Frontier is a limited liability company that is formed under the laws of Colorado and is authorized to conduct business in Kentucky.

6. Kentucky Frontier does not presently own any facilities that provide utility service in the Commonwealth of Kentucky, but operates the facilities of Floyd County Gas and Mike Little Gas under the terms of a Services Agreement with each entity.

7. Kentucky Frontier has entered into an agreement to purchase the assets of Belfry Gas and the rights to serve the estimated 300 farm tap customers that Alert Gas presently serves.

8. On May 25, 2005, Floyd County selected Kentucky Frontier as the successful bidder on the public sale of Floyd County Gas's assets.

9. In 2005 Kentucky Frontier entered into an agreement with Wilma Ison, Elam's sole shareholder, to purchase the outstanding stock of Elam.

10. Kentucky Frontier has entered into an agreement with the Miki Thompson Successor Trust and the Winnie L. Greer Successor Trust to purchase the outstanding stock of Mike Little Gas.

11. In Case No. 2005-00348,³ the Commission authorized Kentucky Frontier's acquisition of Belfry Gas, Floyd County Gas, Elam, and Mike Little Gas.

12. Following Commission action in Case No. 2005-00348, Kentucky Frontier was unable to complete the proposed acquisition because of GOLD's suspension of its financing activities.

13. Upon GOLD's resumption of financing activities, Kentucky Frontier amended the features of the plan of acquisition that the Commission had previously approved. Among these amendments are:

a. A reduction in the estimated cost of the proposed acquisition from \$3.4 million to \$2.9 million.

b. In lieu of borrowing \$1.5 million from GOLD and \$570,000 from outside sources to finance the proposed acquisition of debt, Kentucky Frontier will use equity and a \$1.7 million loan from Community Trust Bank, Inc. The proposed loan from Community Trust Bank is for a 10-year period.

³ Case No. 2005-00348, The Application of Kentucky Frontier Gas. LLC, Belfry Gas, Inc., Floyd County Gas (East Kentucky Utilities, Inc.), Elam Utility Company, Inc., and Mike Little Gas Company for Approval of Transfer and Acquisition of Assets and Stock and Issuance of a Certificate of Public Convenience and Necessity, If Necessary (Ky. PSC Oct. 28, 2005).

c. Kentucky Frontier will acquire \$1.34 million of debt instruments that GOLD holds on the Four Utilities rather than the previous amount of \$1.46 million.

d. Kentucky Frontier's proposed capital structure ratio is 40 percent equity/60 percent long-term debt rather than 30 percent equity/70 percent long-term debt.

e. Gilmer Mickey and Don Silversmith will not have an ownership interest in Kentucky Frontier. Robert Oxford, who previously had no ownership interest, will have a 30 percent interest. The ownership interest of Larry Rich and Steven Shute has increased, while the ownership interest of Industrial Gas Services, Inc., of which Robert Oxford is the president, has decreased.

f. The plan now includes the acquisition of B & H and Johnson County Gas and the acquisition of all debt instruments that those utilities have issued to GOLD.

14. Kentucky Frontier has reached an agreement with GOLD to acquire the debt of Floyd County Gas, Elam, Mike Little Gas, B & H, and Johnson County for \$800,000.

15. Kentucky Frontier does not have an agreement with B & H or Johnson County for the acquisition of either utility's assets or stock.

16. Wilma Ison has repudiated her previous agreement with Kentucky Frontier for the sale of her Elam stock and considers the agreement void.

17. Kentucky Frontier estimates the total acquisition cost of all facilities to be \$2.7 million and the total project cost to be \$2.9 million, which includes the cost of regulatory approvals and initial system upgrades.

18. Upon completion of the proposed transactions, the following persons will have ownership interests in Kentucky Frontier: Industrial Gas Services, Inc. (10 percent); Larry Rich (20 percent); Steven Shute (40 percent); and Robert Oxford (30 percent).

19. Other than to establish a single Gas Cost Recovery Account, Kentucky Frontier does not propose any immediate changes to the rates, regulations, or conditions of service of the Four Utilities.

20. Kentucky Frontier's management has extensive experience in the operation and management of gas pipeline and distribution systems.

21. The consolidation of two or more of the utilities in question will likely result in greater economies of scale, reduce wasteful duplication of costs and efforts, and result in a greater degree of service.

CONCLUSIONS OF LAW

Based upon the above findings of fact, the Commission makes the following conclusions of law:

1. Belfry Gas, Floyd County Gas, Elam, Mike Little Gas, B & H, and Johnson County are utilities subject to Commission jurisdiction.⁴

2. Kentucky Frontier is not a utility and therefore is not currently subject to Commission jurisdiction.⁵

3. Kentucky Frontier is a "person" for purposes of KRS Chapter 278.⁶

⁴ KRS 278.010(3)(b).

⁵ KRS 278.010(3).

⁶ KRS 278.010(2).

4. KRS 278.020(5) provides that “[n]o person shall acquire or transfer ownership of, or control, or the right to control, any utility under the jurisdiction of the commission . . . without prior approval by the commission.” As Kentucky Frontier is a person and proposes to acquire ownership of the above-named utilities, this statute is applicable to and requires Commission approval of the proposed transfer.

5. KRS 278.020(6) provides that “[n]o individual, group, syndicate, general or limited partnership, association, corporation, joint stock company, trust, or other entity (an “acquirer”), whether or not organized under the laws of this state, shall acquire control, either directly or indirectly, of any utility furnishing utility service in this state, without having first obtained the approval of the commission.” As Kentucky Frontier proposes to acquire ownership of the above-named utilities, this statute is applicable to and requires Commission approval of the proposed transfer.

6. When a significant period of time has elapsed since Commission approval of a proposed acquisition of control of a utility and the proposed acquisition has not occurred and significant changes in the proposed plan of acquisition have occurred, the Commission’s approval of the proposed acquisition should be deemed to have lapsed and a new application for such authority should be made.

7. Given the circumstances set forth in Kentucky Frontier’s amended application, the Commission’s prior approval of the acquisition of the Four Utilities has lapsed and is no longer effective.

8. Kentucky Frontier has the financial, technical, and managerial abilities to provide reasonable service to the present customers of Belfry Gas, Floyd County Gas, and Mike Little Gas.

9. The proposed transfers of Belfry Gas, Floyd County Gas, and Mike Little Gas are in accordance with law, for a proper purpose and consistent with the public interest.

10. Absent extraordinary circumstances, Commission approval of a transfer of control or acquisition of a utility is not in the public interest when the applicant for such approval lacks an agreement with the utility or the majority of its shareholders for such transfer or acquisition, or if it has not obtained judicial authorization for such acquisition.⁷

11. Based upon Kentucky Frontier's lack of an agreement with either B & H or Johnson County Gas and Ms. Ison's repudiation of her agreement with Kentucky Frontier, Kentucky Frontier's proposed acquisition of control of Elam, B & H, and Johnson County is not currently in the public interest and should be denied without prejudice.

IT IS THEREFORE ORDERED that:

1. The record in Case No. 2005-00348 is incorporated by reference into the record of this proceeding.

2. Kentucky Frontier's proposed acquisition of control of Belfry Gas, Floyd County Gas and Mike Little Gas is approved.

3. Kentucky Frontier's proposed acquisition of control of Elam, B & H, and Johnson County is denied without prejudice.

⁷ Examples of appropriate judicial authorization include bankruptcy and foreclosure proceedings. While a judicial order directing the transfer may exist, KRS 278.020(5) and (6) require that such orders must be conditioned upon Commission approval of the transfer and acquisition.

4. Commission authorization of the proposed acquisition of control of Belfry Gas, Floyd County Gas and Mike Little Gas is effective for one year from the date of this Order and shall lapse for any of the approved acquisitions that have not been completed within this time period.

5. Within 10 days of completion of each approved acquisition, Kentucky Frontier shall notify the Commission in writing of the completion thereof.

6. Within 10 days of the completion of each approved acquisition, Kentucky Frontier shall file a signed and dated adoption notice in accordance with 807 KAR 5:011, Section 11.

7. Within 10 days of the filing of each adoption notice, Kentucky Frontier shall issue and file with the Commission in its own name each utility's tariff, or such other tariff as it proposes to put into effect in lieu thereof, in the form prescribed in 807 KAR 5:011, Section 11.

8. Within 20 days of the completion of each of the proposed transfers, Kentucky Frontier shall file the journal entries it proposes to record the approved acquisition. The acquisitions shall be recorded in accordance with the Uniform System of Accounts.

9. Nothing in this Order shall be construed as authorizing rate-making treatment of any plant acquisition adjustment and the recovery of any cost or expense associated with the proposed acquisitions of control in Kentucky Frontier's general rates. These issues are deferred until Kentucky Frontier's next rate case proceeding.

10. Each utility that ceases to exist as a result of the proposed acquisition by Kentucky Frontier shall be responsible for submitting to the Commission its financial and

statistical report, as described in 807 KAR 5:006, Section 3, for the period in calendar year 2008 in which it owned and operated its natural gas distribution system.

11. In the event that Kentucky Frontier commences legal proceedings against Elam, B & H, or Johnson County to enforce its rights under any agreement that any of these utilities entered with Kentucky Frontier or with GOLD:

a. It shall at the commencement of such proceedings notify the Commission of its action.

b. It shall advise the court in which the proceedings have been commenced that KRS 278.020(5) and (6) require Commission approval of any judicially directed transfer of ownership of facilities if such transfer constitutes a transfer of control of a utility.

12. In the event Kentucky Frontier obtains judicial authorization to acquire the assets of Elam, B & H, or Johnson County as a result of any legal proceeding, it shall apply for Commission approval prior to the actual acquisition of control of such assets.

13. Within 180 days of completion of the acquisition of Belfry Gas, Floyd County Gas, and Mike Little Gas, Kentucky Frontier shall file with the Commission system maps that reflect the location of its gas distribution mains and associated facilities.

14. Elam's request for removal of any debt instruments that Elam has issued to GOLD from the agreement between Kentucky Frontier and GOLD is denied for lack of jurisdiction.

Done at Frankfort, Kentucky, this 25th day of November, 2008.

By the Commission

ATTEST:

Executive Director