PETITION OF
THE NARRAGANSETT ELECTRIC COMPANY
AND
SOUTHERN UNION COMPANY
FOR APPROVAL OF
PURCHASE AND SALE OF ASSETS

DOCKET NO. D-06-13
BEFORE THE RHODE ISLAND DIVISION OF
PUBLIC UTILITIES AND CARRIERS

TESTIMONY AND EXHIBITS
OF DAVID J. EFFRON

ON BEHALF OF THE

ADVOCACY SECTION OF
THE DIVISION OF PUBLIC UTILITIES AND CARRIERS

JUNE 19, 2006

DIVISION DOCKET NO. D-06-13
DIRECT TESTIMONY
OF DAVID J. EFFRON

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I. STATEMENT OF QUALIFICATIONS

Q. Please state your name and business address.

A. My name is David J. Effron. My business address is 386 Main Street, Ridgefield, Connecticut.

Q. What is your present occupation?

A. I am a consultant specializing in utility regulation.

Q. Please summarize your professional experience.

A. My professional career includes over twenty-five years as a regulatory consultant, two years as a supervisor of capital investment analysis and controls at Gulf & Western Industries and two years at Touche Ross & Co. as a consultant and staff auditor. I am a Certified Public Accountant and I have served as an instructor in the business program at Western Connecticut State College.

Q. What experience do you have in the area of utility rate setting proceedings?

A. I have analyzed numerous electric, gas, telephone, and water filings in different jurisdictions. Pursuant to those analyses I have prepared testimony, assisted attorneys in case preparation, and provided assistance during settlement negotiations with various utility companies.

I have testified in over two hundred cases before regulatory commissions in Alabama, Colorado, Connecticut, Florida, Georgia, Illinois, Indiana, Kansas, Kentucky, Maryland, Massachusetts, Missouri, Nevada, New Jersey, New York, North Dakota, Ohio, Pennsylvania, Rhode Island, South Carolina, Texas, Vermont, Virginia, and Washington.

Q. Please describe your other work experience.

A. As a supervisor of capital investment analysis at Gulf & Western Industries, I was responsible for reports and analyses concerning capital spending programs, including project analysis, formulation of capital budgets, establishment of accounting procedures, monitoring capital spending and administration of the leasing program. At Touche Ross & Co., I was an associate consultant in management services for one year and a staff auditor for one year.

Q. Have you earned any distinctions as a Certified Public Accountant?

A. Yes. I received the Gold Charles Waldo Haskins Memorial Award for the highest scores in the May 1974 certified public accounting examination in New York State.

Q. Please describe your educational background.

A. I have a Bachelor's degree in Economics (with distinction) from Dartmouth College and a Masters of Business Administration Degree from Columbia University

Q. Have you participated in other cases before the Rhode Island Public Utilities Commission or the Division of Public Utilities and Carriers that involved the merger or acquisition of public utilities providing service in Rhode Island?

A. Yes. I was a consultant to the Advocacy Section of the Division in Docket Nos. 2930 and 3401 before the Rhode Island Public Utilities Commission. Docket No. 2930 involved the acquisition of the former Eastern Utilities Associates by New England Electric System (now National Grid USA, subsequent to its acquisition by National Grid), the merger of the former Blackstone Valley Electric and Newport Electric Companies into the Narragansett Electric Company, and the establishment of a rate plan for the merged entity in Rhode Island. Docket No. 3401 involved the acquisition of the former Providence Gas Company and Valley Gas Company by Southern Union Company, the merger of Providence Gas and Valley Gas to create the New England Gas Company, and the establishment of a rate plan for the merged entity in Rhode Island.

II. PURPOSE AND SUMMARY OF TESTIMONY

Q. On whose behalf are you testifying?

A. I am testifying on behalf of the Advocacy Section of the Rhode Island Division of Public Utilities and Carriers.

Q. What is the purpose of your testimony?

A. The Narragansett Electric Company ("Narragansett") and Southern Union Company ("Southern Union"), together "Petitioners", have submitted a petition to the Rhode Island Division of Public Utilities and Carriers ("the Division"), requesting approval for Narragansett to acquire the assets associated with the regulated gas distribution business owned and operated by Southern Union in

Rhode Island as the New England Gas Company ("NEG"). NEG is presently operated as an unincorporated division of Southern Union. If the requested approval is granted, Narragansett will acquire the NEG gas distribution assets and provide gas distribution service in the area presently served by NEG in Rhode Island. The purpose of this testimony is to address consequences of the proposed transaction that could potentially have an adverse effect on rates paid by customers if not addressed and resolved. In particular, I focus on certain accounting implications, revenue requirement matters, and other rate issues associated with the proposed transaction, and I explain why these subjects should be considered by the Division in its determination of whether the proposed acquisition of NEG's assets by Narragansett is consistent with the public interest.

In the preparation of this testimony, I have not read the testimony or exhibits related to any issues that may be addressed by other intervenors in this proceeding. Therefore, I do not take a position on those issues, and the fact that I do address such issues in this testimony should not be interpreted to mean that either the Advocacy Section of the Division or I either support or oppose the positions of the intervenors on those issues.

Q. Please summarize the matters that you are addressing and your recommendations on those matters.

A. The proposed transaction will result in the recording of a substantial acquisition premium. If the acquisition premium were to be incorporated into the ratemaking formula, it would increase the revenue requirement associated with utility cost of service in Rhode Island significantly. As a condition to approval of the merger, Narragansett should agree not to seek any recovery of the acquisition premium in the electric or gas distribution cost of service.

The New England Gas Company rate freeze pursuant to the Settlement in Docket No. 3401 expired on June 30, 2005. Petitioners have stated that Narragansett will be proposing a new rate plan within six months after the closing. The new rate plan should not be approved unless it improves on the present NEG rate plan, and gas distribution rates should be frozen until the Rhode Island Public Utilities Commission ("Commission") renders a decision on the new rate plan.

All transaction costs incurred by National Grid USA (the parent company of Narragansett) and Southern Union should be excluded from the cost of service. Integration costs should be recoverable only to the extent that Narragansett can demonstrate that savings attributable to the acquisition exceed such integration costs.

Narragansett will establish a regulatory asset to offset the additional pension and PBOP liability that will be recorded in association with the acquisition. Recovery of this regulatory asset should be allowed only to the extent that Narragansett can verify that such recovery does not result in greater pension and PBOP expenses in the cost of service than those expenses would be in the absence of the acquisition.

The balance of Accumulated Deferred Income Taxes ("ADIT") deducted from the NEG rate base for ratemaking purposes will be eliminated as a result of the acquisition. If a mechanism is not established to offset the effect of the elimination of the ADIT or hold ratepayers harmless from the revenue requirement effect of the loss of this rate base deduction, the proposed transaction will result in adverse effect on rates paid by customers.

Southern Union has stated that it is "required" to close the proposed transaction on or before August 25, 2006. The acquisition will not necessarily terminate if does not close by that date. However, there are advantages to closing the acquisition by August 25, 2006. If the Division determines that the proposed transaction is consistent with the public interest, a target closing date on or before August 25, 2006 is not an unreasonable objective.

III. ISSUES IN THE PROPOSED TRANSACTION

A. ACQUISITION PREMIUM (GOODWILL)

Q. How will Narragansett account for the acquisition of New England Gas Company's Rhode Island operations?

A. Narragansett will acquire the Rhode Island assets and assume the related liabilities of NEG and will operate the acquired assets as a separate division of Narragansett, within a single corporation. The acquired assets of and liabilities on the books of NEG will be adjusted to reflect their fair values as of the date that the acquisition closes. If the purchase price is greater than the fair value of the assets less the fair value of the liabilities (the net book value) of NEG, the difference will be recorded as an acquisition premium, or goodwill.

Q. Is it contemplated that such an acquisition premium will be recorded?

A. Yes. Because it is expected that the NEG assets will be acquired at a premium to the fair value of the net assets being purchased, an acquisition premium will be recorded. The acquisition premium will remain on the books of Narragansett, subject to future evaluation of the premium for impairment.

Q. What is the magnitude of the acquisition premium that will be recorded on Narragansett's books of account?

A. The exact amount of the acquisition premium is not known at this time. However, Narragansett estimates that the acquisition price of $575 million (including the assumption of $77 million of NEG debt) will exceed the fair value of the net assets being acquired by approximately $250 million. This acquisition premium will appear as goodwill on the balance sheet of Narragansett, with the offsetting entry to paid-in-capital, a component of common equity.

Q. Has Narragansett determined how this goodwill will be treated for ratemaking purposes in the determination of its electric and gas delivery rates?

A. In response to Division Data Request 6-2, Narragansett stated that "It is not anticipated that the acquisition premium would be included in the determination of the revenue requirement." However, this representation appears to be contingent on the establishment of a rate plan similar to that developed in Docket No. 2930, wherein shareholders were allowed to retain a share of proven merger savings to cover the costs associated with the acquisition of EUA by NEES and the acquisition of NEES by National Grid. Based on Narragansett's response, it appears to be reserving the option of including the acquisition premium in the determination of the revenue requirement if negotiations do not result in a satisfactory rate plan or if a satisfactory rate plan is not ultimately approved by the Commission.

Q. What would the effect on revenue requirements be if the goodwill recorded in association with the merger were recognized for ratemaking purposes in setting electric or gas distribution rates?

A. The effect would be a substantial increase to revenue requirements. The increase in revenue requirements would result from (1) including the goodwill in rate base and (2) the increase to the common equity ratio in the capital structure related to the recording of the goodwill.

Q. Can you illustrate what the approximate effect on revenue requirements might be if the goodwill is recognized for ratemaking purposes?

A. Yes. On my Schedule DJE-1, I present an estimate of the effect on the gas division revenue requirements if Narragansett sought to include goodwill in the determination of the cost of gas service. This estimate assumes a rate base of $243 million exclusive of goodwill (an estimate, based on the most recent NEG earnings sharing calculation) and $250 million of goodwill booked as a result of the merger. Thus, if the goodwill is included in rate base, the rate base would increase from $243 million to $493 million.

In addition, the booking of goodwill affects the capital structure. Based on the present earnings sharing formula NEG's capital structure contains 43.6%

common equity. If the goodwill were assigned to the NEG capital structure for ratemaking purposes, the result would be a capital structure with a common equity ratio of 72.2%. For the purpose of this example, the cost of common equity is based on the settlement return on common equity of 11.25% presently specified in the NEG earnings sharing formula.

Exclusive of the effect of recording the goodwill, the revenue requirement related to the return on rate base, including the income taxes on the equity component of the return, is $28.4 million. The inclusion of goodwill in rate base, and the related effect of the goodwill on the capital structure, increases the revenue requirement related to the return on rate base to $76.8 million. In other words, recognition of the goodwill for ratemaking purposes would increase NEG's annual revenue requirement by some $48 million.

Q. In theory, is it appropriate to recognize goodwill booked as a result of a merger or acquisition for ratemaking purposes?

A. No. As a general matter, any acquisition premium is the result of a transfer of wealth from one group of shareholders to another group of shareholders. The excess over net book value being paid for the acquired entity is based on capitalization of the expected future earnings in excess of the cost of capital. In theory, if the rate of return earned by an acquired utility is equal to its actual cost of capital, then none of the acquisition premium is properly allocable to the acquired utility. In any event, the price being paid in excess of net book value is a matter between the shareholders of the buyer and seller and should not be the responsibility of ratepayers. The acquisition premium in this case is the result of the excess of the purchase price over its net book value, something that was determined by the shareholders of the National Grid and Southern Union and is not related to the cost of providing service to NEG's customers.

Any detriment to National Grid's shareholders resulting from the premium being paid for NEG's assets is exactly offset by a benefit to Southern Union's shareholders. If it is assumed that any of the premium being paid is related to the acquisition of assets devoted to providing public service, it makes as much sense to argue that NEG's customers have a right to the benefit of the premium being received as it does to argue that National Grid's shareholders have a right to recover the cost of the premium being paid.

Q. In addition to these general principles, are there any reasons particular to this case why the goodwill should be excluded from the ratemaking process?

A. Yes. It is my understanding that in order to approve the proposed transaction, the Division must find that it is consistent with the public interest. One key element in such a finding must be that the proposed transaction will have no adverse impact on existing rates. To achieve this end, any acquisition-related costs must be offset by savings attributable to the acquisition. So far, Narragansett has not explicitly quantified any savings resulting from the merger of a magnitude that would offset the revenue requirement effect of the acquisition premium. Even under the most optimistic forecasts, I do not believe that the annual savings allocable to NEG will be anything remotely approaching the revenue requirement effect of the goodwill.

Thus, if the goodwill, or any significant portion of the goodwill, is explicitly recognized for ratemaking purposes, there is no reasonable likelihood that savings attributable to the acquisition would be adequate to offset the additional revenue requirements imposed on ratepayers by the recognition of the goodwill. Accordingly, the goodwill should not be recognized for ratemaking purposes under any circumstances, regardless of the outcome of negotiations to establish a rate plan.

B. PRESENT NEG RATE PLAN

Q. Please describe the rate plan under which NEG is presently operating.

A. The rate plan under which NEG is presently operating was established pursuant to the Settlement Agreement approved by the Commission in Docket No. 3401 ("Settlement"). The Settlement originally froze rates from July 1, 2002 through June 30, 2005, subject only to certain defined exogenous events (none of which occurred during the rate freeze period). NEG was permitted to file a base rate proposal to change rates for service after June 30, 2005, and other parties were permitted to file a complaint requesting a cost of service review to reduce rates after that date.

In addition, the Settlement established an earnings sharing mechanism ("ESM") whereby earnings in excess of an 11.25% return on equity would be shared with customers. The ESM was in effect during the rate freeze period and continues in effect subsequent to the rate freeze period, until June 30, 2010.

Q. With the rate freeze having expired, is there any indication that NEG will be filing a base rate proposal to change rates?

A. No. The last ESM calculation, covering the twelve months ended June 30, 2005, showed NEG still earning a return on equity in excess of 11.25%. Based on that, NEG does not appear to be experiencing a revenue deficiency. On the other hand, the return on equity was not so high as to imply that the NEG distribution rates are clearly excessive, so no other party has filed a complaint.

Q. Will this rate plan continue in effect?

A. Yes. The sale of NEG assets to Narragansett will not, by itself, affect the obligations of the parties to the Settlement in Docket No. 3401. However, Narragansett has stated that it plans to file new rate plan with the Commission within six months of the after the closing. If there is to be any chance that the new rate plan will be approved, it must produce benefits to customers above and beyond the present rate plan. As the present plan remains in effect unless modified, there would be no reason to approve a new plan unless it is an improvement over the present plan.

In addition, as noted above, prior to the initiation of the talks between National Grid and Southern Union, there was no indication that NEG was experiencing a revenue deficiency. Were NEG or Narragansett to request a rate increase for gas distribution service prior to a final decision on the rate plan that Narragansett plans to submit, it would raise a concern that the rate increase was related to the change in ownership of NEG. Therefore, although the rate freeze established in Docket No. 3401 has expired, Narragansett and NEG should agree not to request any change in gas distribution rates prior to a resolution of the rate plan that Narragansett will be submitting within six months after the closing.

C. TRANSACTION AND INTEGRATION COSTS

Q. Are costs being incurred costs to complete the proposed transaction?

A. Yes. National Grid and Southern Union are incurring costs related to the proposed transaction. The costs consist of legal fees, consulting fees, employee costs, and miscellaneous expenses. Southern Union will also incur retention bonuses (estimated at about $300,000) to be paid to employees to assist in achieving a smooth transition. Because NEG employees will receive offers of employment from Narragansett, it is not expected that there will be any severance payments to NEG employees. Southern Union estimates that it will incur approximately $1 million in costs to complete the proposed transaction. Through April 30, 2006, National Grid had incurred approximately $1.4 million in costs associated with the proposed purchase and expects to incur additional costs of approximately $1 million to complete the transaction. The National Grid amounts include integration costs.

Q. Should recovery of the transaction costs be included in the revenue requirement of Narragansett's electric or gas operations?

A. No. The transaction costs are expenditures being incurred on behalf of shareholders to consummate the merger, not costs being incurred to achieve savings. That is, they relate to the change in ownership of NEG, not to the operation of the merged entity. The transaction costs would be incurred even if the merger did not result in any cost savings.

Narragansett and Southern Union would not be proposing this merger if they did not believe that the merger would be in the best interests of their shareholders. Thus, it is reasonable to infer that the transaction costs are being incurred for the benefit of those shareholders. Accordingly, the transaction costs should be treated as shareholder costs that are not recoverable from ratepayers. Both National Grid and Southern Union should track the transaction costs as incurred. The transaction costs incurred by National Grid and Southern Union should be excluded from any costs that go into the determination of rates, either as part of the earnings sharing mechanism or in the determination of revenue requirements in the context of a rate case.

Q. Do Southern Union and Narragansett agree?

A. They appear to agree. Southern Union has stated that the transaction costs will be recorded at the Southern Union level and will not be recorded on the books of NEG or charged back to NEG for ratemaking purposes (response to Division Data Request 6-7). Narragansett has stated that transaction costs will be charged to a deferred balance sheet account (at the National Grid level based on the response to Division Data Request 6-8) and will become part of the costs to acquire the NEG assets, which implies that the costs will not be recoverable in rates. However, it has not yet been determined how much of the National Grid total costs are considered to be integration related and therefore assignable to Narragansett.

Q. Should the integration costs be recoverable in rates?

A. To the extent that integration costs result in the achievement of savings, such costs should be potentially recoverable. If Narragansett can demonstrate that the acquisition has resulted in quantifiable savings, then the integration costs should be potentially recoverable as an element of the cost of service, to the extent that the costs do not exceed the savings. Alternatively, Narragansett could retain a portion of the demonstrated savings, which would be deemed to cover the integration costs. Under this latter approach, there would be no reason to distinguish between the transaction and integration costs as there would be no explicit recovery in the cost of service of either type of cost.

D. PENSION AND PBOP LIABILITIES

Q. Will the merger affect the liabilities for pensions and postretirement benefits other than pensions ("PBOP") recorded on the balance sheet of NEG?

A. Yes. NEG accounts for pensions pursuant to Statement of Financial Accounting Standards ("SFAS") 87 and for PBOP pursuant to SFAS 106. These accounting standards require certain actuarial assumptions to determine the pension and PBOP liabilities and periodic costs. The assumptions include discount rates, return on invested funds, mortality, inflation, and other factors that go into the calculation of the liabilities and the periodic costs. The actual experience in the real world never exactly matches the actuarial assumptions, and the assumptions will have to be adjusted from time to time based on actual experience and changing circumstances. SFAS 87 and SFAS 106 do not require that the entire difference between the assumptions and actual experience or the cumulative effect of changes in actuarial assumptions be recognized immediately for financial reporting purposes. Rather, the effect of these deviations is recognized over time. However, merger accounting requires that that assets and liabilities be stated at their fair value at the time of the merger or acquisition.

In the case of NEG, this will require that the balance sheet liabilities for pensions and PBOP be increased to their fair value when the acquisition closes. In effect, rather than recognizing the increases in the liabilities over time through increased annual expense, the increases in the liabilities are recognized instantaneously at the time of the acquisition. This reduces the pension and PBOP expenses prospectively below what these expenses would be in the absence of the acquisition.

Q. How does Narragansett propose to address the restatement of the pension and PBOP liabilities for ratemaking purposes?

A. Narragansett will establish a regulatory asset to offset the additional pension and PBOP liability that will be recorded in association with the acquisition (responses to Division Data Requests 7-5 and 7-6). This mechanism entails offsetting entries, an increase to the accrued liabilities and the establishment of a regulatory asset equal to the incremental pension and PBOP liabilities. The purpose of this accounting treatment should be to maintain the periodic pension expense and periodic PBOP expense in the cost of service at the same level as would exist in the absence of the acquisition.

Q. Do you agree that the proposed accounting treatment is appropriate?

A. Yes. However, Narragansett should be required to verify that the proposed accounting treatment accomplishes its stated goal in future rate cases. That is, the recording of the pension and PBOP regulatory asset should not increase the NEG revenue requirement above what it would be in the absence of the acquisition. For example, the regulatory asset should not be included in rate base unless the incremental liability is treated as an offsetting rate base deduction. If the amortization of the regulatory asset is included in operating expenses, then Narragansett should be required to verify the amortization does not result in the pension and PBOP expense being greater than it would have been in the absence of the acquisition.

Q. How could Narragansett verify the amortization does not result in the pension and PBOP expense being greater than it would have been in the absence of the acquisition?

A. The pension expense pursuant to SFAS 87 and the PBOP expense pursuant to SFAS 106 should be calculated on a pro forma basis as if the balance sheet liabilities for pensions and PBOP had not been restated to their fair value at the time of the merger. That pro forma pension and PBOP expense should then be compared to the actual test year pension and PBOP expense plus the amortization of the regulatory asset is included in operating expenses. If the pro forma pension and PBOP expense is equal to the actual pension and PBOP expense plus the amortization of the regulatory asset, then the pension and PBOP accounting can be deemed to have achieved its stated purpose.

E. ACCUMULATED DEFERRED INCOME TAXES

Q. Will the proposed transaction affect the balance of accumulated deferred income taxes ("ADIT") deducted from plant in service for the purpose of determining the NEG rate base used to establish rates and in its earnings sharing calculation?

A. Yes. The transaction is being structured as a purchase and sale of assets. At the time that Narragansett acquires the assets, it will establish a new tax basis for those assets, including plant in service, equal to the acquisition cost of those assets. As the tax basis at the time of acquisition will equal the book basis, there will be no balance of ADIT at that time. The balance of ADIT deducted from the NEG rate base for ratemaking purposes will be eliminated.

Q. What is the effect of eliminating the balance of ADIT at the time of the acquisition by Narragansett?

A. As of June 30, 2005, the balance of ADIT deducted from plant in service for the purpose of determining the NEG rate base used in the earnings sharing mechanism was approximately $35 million. Based on the threshold rate of return in the ESM, this rate base deduction has the effect of reducing the NEG revenue requirement by approximately $4 million. Thus, elimination of this rate base deduction, other things equal, will increase the NEG revenue requirement by $4 million in the first year after the merger. The effect of the elimination of the ADIT at the time of the acquisition will diminish over the years, as the deferred taxes on the acquired assets re-accumulate. In addition, the balance of ADIT existing at the time of acquisition would reverse over time even in the absence of the acquisition. However, in the years immediately following the proposed transaction, the loss of the ADIT will impose additional costs on ratepayers.

Q. Absent the establishment of some special mechanism, does elimination of the ADIT have the potential to cause the acquisition to result in an adverse impact on rates?

A. Yes. The initial increase to the revenue requirement resulting from the elimination of the ADIT exceeds the synergy savings that have so far been identified. Thus, absent the establishment of some compensatory mechanism, the proposed transaction will adversely affect ratepayers in the early years after the transaction. Unless Narragansett can guarantee synergy savings that will at least equal the effect of elimination of the ADIT or can formulate a mechanism to hold ratepayers harmless from the elimination of the ADIT, the proposed transaction will have an adverse affect on rates paid by customers.

F. TRANSACTION CLOSING DATE

Q. On page 7 of his direct testimony, Southern Union witness Marshall stated that Southern Union is "required" to close the proposed transaction on or before August 25, 2006. Could you please elaborate on this "requirement"?

A. Yes. Section 9.1(e) of the Purchase and Sale Agreement ("P&S") specifies August 25, 2006 as the "Upset Date." What this means is that if the transaction does not close by that date, either party can propose to terminate the transaction. However, this section of the P&S also stipulates that if the only reason that the transaction has not closed by the Upset Date is the failure to obtain necessary government approvals, but such approvals are reasonably capable of being obtained after that date, the other party has the option to extend the Upset Date in thirty day increments up to an aggregate of 120 days. After that, the closing date could only be extended by mutual consent.

Thus, there is no formal requirement that the transaction must necessarily close by August 25, 2006. For example, if the only reason that the closing has not taken place by August 25, 2006 is failure to obtain Division approval, but it appears that such approval could be forthcoming shortly after that date, the closing date can be extended at the option of either party.

Q. What is the significance of the August 25, 2006 date?

A. If transaction closes by August 28 (the first business day after August 25), the seller, Southern Union, will be eligible for favorable tax treatment, known as "like-kind exchange," on the property being sold. This favorable tax treatment would entail the deferral of federal income taxes payable on any gain on the sale of NEG assets. Section 11.2 of the Purchase and Sale Agreement states that Narragansett will cooperate with Southern Union in its efforts qualify the transaction as a like-kind exchange; however qualification of the transaction as a like-kind exchange is not a condition to closing.

Q. Would qualification of the transaction as a like-kind exchange affect customers?

A. No, the tax benefits would accrue to the Seller, Southern Union, not customers. However, both the Buyer and Seller have established August 25 as the goal for closing the transaction and the date around which transaction activities have been planned. Accordingly, closing by that date may allow for the achievement of a more orderly transition, while delay could mean the disruption of the transition and integration of operations, resulting in additional costs. Closing after that date means that both parties will continue to incur transaction costs and that realization of potential benefits of the transaction may be delayed.

Q. Does this conclude your direct testimony?

A. Yes.

NARRAGANSETT ELECTRIC COMPANY
NEW ENGLAND GAS COMPANY
EFFECT OF GOODWILL ON REVENUE REQUIREMENT
($000)

	Without Goodwill	With Goodwill
Rate Base	$243,000	$493,000
Rate of Return, Grossed up for Income Taxes	11.68%	15.58%
Revenue Requirement for Return	$ 28,385	$ 76,788

Rate of Return without Goodwill

	Balance	Weight	Cost Rate	Weighted Cost	Pre-Tax Cost
Short Term Debt	$ 21,384	8.80%	3.13%	0.28%	0.28%
Long Term Debt	111,051	45.70%	7.81%	3.57%	3.57%
Preferred Stock	4,617	1.90%	9.93%	0.19%	0.29%
Common Equity	105,948	43.60%	11.25%	4.91%	7.55%
Total	$243,000	100.00%		8.94%	11.68%

Rate of Return with Goodwill

	Balance	Weight	Cost Rate	Weighted Cost	Pre-Tax Cost
Short Term Debt	$ 21,384	4.34%	3.13%	0.14%	0.14%
Long Term Debt	111,051	22.53%	7.81%	1.76%	1.76%
Preferred Stock	4,617	0.94%	9.93%	0.09%	0.14%
Common Equity	355,948	72.20%	11.25%	8.12%	13.54%
	$493,000	100.00%		10.11%	15.58%

Sources: NEG Earnings Sharing Calculation, RIPUC Docket No. 3690
Response to Division Data Request 6-1