STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS BEFORE THE DIVISION OF PUBLIC UTILITIES AND CARRIERS

In Re: Joint Petition for Purchase and Sale of Assets by The Narragansett Electric Company and Southern Union Company — Docket No. D-06-13

POST-HEARING MEMORANDUM OF SOUTHERN UNION COMPANY IN SUPPORT OF THE JOINT PETITION OF SOUTHERN UNION COMPANY AND THE NARRAGANSETT ELECTRIC COMPANY

Southern Union Company ("Southern Union") submits this post-hearing memorandum in support of the Joint Petition filed by Southern Union and The Narragansett Electric Company ("Narragansett") seeking approval, pursuant to Rhode Island General Law § 39-3-25, of the purchase by Narragansett of the assets associated with the regulated gas distribution business owned and operated by Southern Union in Rhode Island.

At a public hearing held on June 29 and 30, 2006, Southern Union and Narragansett demonstrated that the proposed asset sale satisfied the requirements of R.I.G.L. § 39-3-25 because the sale: (i) will benefit Rhode Island ratepayers; and (ii) will not negatively impact Southern Union's ability to pay a potential judgment concerning alleged contamination in the Bay Street Area of Tiverton, Rhode Island. The first premise is unchallenged in this proceeding – no party disputed that the proposed sale is in the best interests of the ratepayers. The Attorney General, the Rhode Island Department of Environmental Management ("RIDEM") and the Town of Tiverton ("Tiverton") challenged the second premise, but failed to present any competent evidence to support their contention. The record evidence

overwhelmingly demonstrates that the proposed sale will not impact Southern Union's ample ability to pay a potential Tiverton judgment.

Based on the evidence presented at the hearing, as well as the arguments set-forth below, the Division of Public Utilities and Carriers (the "Division") should unconditionally approve the Joint Petition.

Background

On March 16, 2006, Narragansett and Southern Union filed a joint petition with the Division seeking approval of the sale of Southern Union's Rhode Island assets to Narragansett.

On May 4, 2006, the Division permitted the intervention of the Attorney General, RIDEM and Tiverton for the limited purpose of "seeking assurances that the proposed asset sale does not negatively impact Southern Union's ability to pay for remedial actions in the event it is found liable for any of the contamination in Tiverton." (See Division Order No. 18591 ("Order") at 16.) The Division recognized that determining liability for the alleged contamination was beyond the scope of the Division proceeding. (Id. at 14-20.) The Division further noted that none of the intervenors sought to require Southern Union to place money in escrow to fund any possible remediation. (See Division Intervention Hearing Transcript ("Hr. Tr.") at 53.)[1]

The record for the public hearing includes testimony of the Joint Petitioners, the Division, the Attorney General, Tiverton and the Wiley Center, as well as documentary exhibits, which collectively demonstrate that:

[1] The George Wiley Center ("Wiley Center") was also permitted to intervene. As the Wiley Center's intervention did not address the potential impact of the proposed asset sale on Southern Union's ability to fund a remediation, it is not addressed in this memorandum.

(a) the proposed transaction will provide benefits to customers, and therefore, meets and exceeds the legal standard for approval by the Division under R.I.G.L. § 39-3-25;

(b) there is no legal or factual basis to support a finding that approval of the transaction will have a negative impact on Southern Union's ability to pay for remedial actions in the event it is found liable for any of the contamination in Tiverton; and

(c) there is no legal or factual basis to require Southern Union to post an escrow or other security relating to the Tiverton site or to impose any other related conditions on the approval of the Joint Petition.

Each of these points is addressed in detail below.

Standard of Review

Under R.I.G.L. § 39-3-25, the Division has the authority to approve the conveyance of utility assets from one utility to another if the Division is satisfied that "the facilities for furnishing service to the public will not thereby be diminished, and that the purchase, sale, or lease and the terms thereof are consistent with the public interest . . . ." The Division has stated that its role in applying § 39-3-25 is to: (i) examine the record evidence for confirmation that ratepayers will not be harmed; and (ii) to look for substantiation that ratepayers would actually benefit from the transaction. See In re: Petition of Valley Gas Company, et al., Docket No. D-00-02; In re: Petition of Providence Gas Energy Corp., et al., Docket No. D-00-03 (2000). In this case, the Division broadened its traditional scope of inquiry to include a determination that the proposed asset sale does not negatively impact Southern Union's ability to pay for remedial actions in the event it is found liable for the contamination in Tiverton. (Order at 16.)

Legal Analysis

(a) The Proposed Transaction Meets And Exceeds The Legal Standard For Approval Of Utility Transfers.

In this case, the record shows that customers will likely experience benefits as a result of the transaction and, at the very least, will suffer no net harm. Specifically, Narragansett's witnesses testified (both on direct and rebuttal) that, through the consolidation of operations, gross annual savings estimated at $4.9 million per year for Rhode Island customers may be attainable by virtue of the transaction. (See, e.g., Joint Petitioners' Exhibit 1, Testimony of R. Gerwatowski ("Gerwatowski Testimony") at 8; Narragansett Exhibit 1, at 2; Narragansett Exhibit 3, response to DIV 1-9, at 1.) Narragansett has also identified other benefits encompassing cost savings, improved business operations and service-related enhancements. (See, e.g., Joint Petitioners Exhibit 1, Gerwatowski Testimony and Testimony of Michael Laflamme ("Laflamme Testimony"); Narragansett Exhibit 1; Narragansett Exhibit 3.)

The testimony of the Division's witnesses supports this determination, with their substantive commentary restricted to various ratemaking issues that may be implicated in the development of a rate plan following the Division's approval of the proposed transaction. (See, e.g., Gerwatowski Testimony and Laflamme Testimony; Narragansett Exhibit 1; Narragansett Exhibit 3; June 29 Public Hearing Transcript ("June 29 Tr.") at 78-163.) In fact, aside from the Tiverton issue and the narrow issue raised by the Wiley Center relating to the potential for the consolidation of electric and gas bills, the testimony of the Joint Petitioners is uncontroverted, and provides a fully adequate basis for the Division's approval of the Joint Petition.

Accordingly, the Division should approve the transaction, finding that there will be no diminution of utility facilities as a result of the transaction, and that the transaction as a whole is in the public interest.

(b) The Proposed Transaction Will Not Diminish Southern Union's Ability To Pay A Judgment If Liability Is Found In The Appropriate Forum(s).

As noted above, the Division agreed to consider whether the proposed asset sale will negatively impact Southern Union's ability to pay for remedial actions if it is found liable for any of the contamination in Tiverton. (Order at 16.) The evidence now before the Division demonstrates that the sale will not impact Southern Union's ability to pay a Tiverton judgment. The undisputed evidence is that Southern Union presently has $7.5 billion in assets and $4.0 billion in debt. The "net spread" of $3.5 billion will remain unaffected by this transaction. (See June 30 Public Hearing Transcript ("June 30 Tr.") at 194-195.) Further, the evidence demonstrates that Southern Union could pay a potential Tiverton judgment in several ways, including: (1) out of the "revolving loan" facility (2) by obtaining additional borrowings, or (3) through the issuance of additional equity or long-term debt instruments. (Id. at 195-197.) The upper range of the potential Tiverton judgment is less than 1% of Southern Union's assets, and less than 2% of Southern Union's outstanding debt. (Id.)[2] The uncontroverted evidence further demonstrates that Southern Union has the financial wherewithal to pay such a judgment, which would have no appreciable impact on Southern Union's financial condition.

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[2] Certain parties stipulated, solely for purposes of this proceeding, that the Hearing Officer could use a range of $30 million to $55 million for the potential cost of remediation of the Bay Street Area in Tiverton. Solely in the context of that stipulation and this proceeding, Southern Union did not object to this stipulation.

It is therefore not surprising that the intervenors abandoned their purported concern that after the sale Southern Union will lack sufficient assets to fund a remediation, and shifted their focus to speculation that at some unknown time in the future Southern Union will engage in unlawful corporate actions to avoid its obligation, if any, to fund a remediation in Tiverton. The theory presented by the Attorney General's witness "imagined" a series of fraudulent transfers of Southern Union's assets to wholly owned subsidiaries or third parties.

The only purported "evidence" proffered by any intervenor on this theory was presented by the Attorney General's witness, Mr. Philip Sussler. Yet, Sussler not only failed to substantiate this theory, but directly contradicted it. Indeed, Sussler's testimony did nothing more than confirm that Southern Union cannot evade its legal obligation through either the Rhode Island asset sale or the formation of wholly owned subsidiaries in the future.[3]

Specifically, Sussler confirmed the validity of the Company's representations, conceding the following:

- When Southern Union merged with Fall River Gas Company ("FRGC"), Southern Union succeeded to whatever environmental liabilities (including CERCLA liabilities) FRGC may have had with respect to Tiverton to the extent that FRGC is found liable for the contamination in Tiverton. (June 30 Tr. at 120-122.)
- Southern Union cannot "avoid" its potential liability under CERCLA in relation to Tiverton by transferring assets (or liabilities) either through a sale or the formation of a subsidiary. (Id. at 120-137.)
- Southern Union's contemplated "Massachusetts Transfer," or any other future transfer of assets through the creation of a subsidiary does not in any way hinder a creditor's ability to satisfy a judgment because the creditor can obtain satisfaction by attaching the parent's stock in its subsidiaries. (Id.)
- There are no facts and no evidence to indicate Southern Union has, plans to, or will transfer or "cabin" its assets to protect them from the reach of any creditor who may obtain a judgment in connection with Tiverton. (Id. at 144.)

[3] In a separate filing, Southern Union has moved to strike/exclude Sussler's testimony. In any event, even if admitted, Sussler's testimony only serves to confirm that Southern Union cannot escape its legal obligation, if any, to fund the remediation in Tiverton.

- Laws in every state prohibiting fraudulent conveyances protect a creditor or potential creditor from a corporate reorganization designed to obstruct the collection of a legitimate judgment. (Id. at 141-147.)
- Laws allowing for "long-arm" jurisdiction and service of process on entities doing business outside of Rhode Island protect a creditor's ability to reach Southern Union, even if it has no assets in the State of Rhode Island. (Id. at 152-154.)[4]
- In addition, there is no rational basis for analogizing Southern Union's position here to the sole case cited by Sussler, i.e., the bankruptcy of W.R. Grace, because the damages in that case exceeded the net worth of the company, causing the company to seek bankruptcy protection. By contrast, the above-referenced maximum liability figure of $55 million represents less than 1% of Southern Union's assets and less than 2% of its debt. (Id. at 148-150, 194-197.)

In the end, Sussler's testimony offers nothing more than innuendo and speculation regarding the possibility that somewhere down the line, Southern Union could (and would) pull off some massive reorganization to avoid the payment of a judgment that is a modest amount in comparison to Southern Union's overall net worth. (Id. at 144.) Sussler admitted he had no facts – none whatsoever – to support his speculation. This type of innuendo and unsubstantiated commentary is not competent evidence and does not provide a basis for a finding by the Division that the proposed transaction will negatively impact Southern Union's ability to fund a remediation in Tiverton, if legally obligated to do so.[5]

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[4]Rule 4(f)(2) of the RIRCP provides that service on a foreign corporation can be made by mail. Rhode Island's long-arm statute and the relevant case law (Del Guidice v. Robbins, 410 F. Supp. 303, 306 (D.R.I. 1976)) demonstrate that Southern Union will continue to be subject to Rhode Island jurisdiction following the asset sale, if that sale is approved by the Division. R.I. Gen. Laws § 9-5-33(a).

[5] As Tiverton's sole witness, David Sousa, submitted no testimony relevant to this proceeding, and lacked any personal knowledge on the matters on which he testified, Southern Union will not further address his testimony. Further, Tiverton's post-hearing memorandum is riddled with misrepresentations and should be disregarded. First, contrary to Tiverton's assertion, while the Settlement Agreement between Southern Union and Stone & Webster (which is not in evidence) addressed alleged contamination of land in Rhode Island and Massachusetts, it in no way constituted an admission by Southern Union that FRGC was liable for the contamination of land in Tiverton or anywhere else. Because insurance companies have an obligation to defend claims based on contentions by third parties, a claim that a payment by an insurer to defend a claim is an admission of liability is "uninformed" at best. Second, Tiverton's claim, both at the hearing and in their Post-Hearing memorandum, that Southern Union had not submitted a plan regarding remediation of the Corey's Lane area of Tiverton is demonstrably false. The evidence, including a letter dated May 5, 2006 (that is in evidence) from RIDEM to Southern Union, demonstrated that Southern Union had, in fact, presented a plan for the remediation of Corey's Lane and that Southern Union continued to work closely with RIDEM on that plan.

In any event, Southern Union has already offered the following stipulations for the record, which directly address any conceivable concern the Division may have:

(i) Upon its merger with FRGC in 2000, Southern Union acquired and succeeded to whatever potential legal liabilities FRGC had at that date relating to environmental contamination that may have existed in the "Bay Street Area" of Tiverton, Rhode Island (the "FRGC Tiverton Liabilities");

(ii) Neither the approval of the Joint Petition in this proceeding, nor the potential transfer of Southern Union's Massachusetts assets to a wholly owned subsidiary ("Massachusetts Transfer") shall alter: (i) Southern Union's liability for the FRGC Tiverton Liabilities; or (ii) Southern Union's legal obligation to satisfy a final (following all appeals) enforceable judgment entered against it arising out of the FRGC Tiverton Liabilities;

(iii) Southern Union shall not assert in any judicial, administrative or other legal proceeding that by reason of the form or structure of its present or planned Massachusetts corporate organization it is not liable for the FRGC Tiverton Liabilities; and

(iv) Nothing in this agreement shall be taken or construed as an admission that FRGC before the Merger, or Southern Union after the Merger, is or was liable or responsible for the environmental issues in the Bay Street Area.

(c) There Is No Legal Or Factual Basis To Support The Creation Of An Escrow Fund.

For these same reasons, there is no basis for the creation of an escrow fund to guarantee payment of a potential Tiverton judgment. The intervenors have utterly failed to prove any need for security. The creation of an escrow account would, therefore, inappropriately deny Southern Union the ability to use its funds for legitimate business purposes and would constitute a penalty unsupported by record evidence and that may be beyond the Division's authority to grant. Requiring an escrow fund would be a form of stealth attachment, without any due process of the kind required in court, including the

substantial burden on the movant to show a likelihood of success on the merits and demonstrated proof of the need for security.[6]

Second, an escrow fund would inappropriately cause Southern Union to set-aside millions of dollars for an indeterminate period, causing injury to Southern Union and its shareholders, and resulting in carrying costs without any ability to recoup them.

Third, an escrow account is unnecessary because the Company has demonstrated that it has adequate funds readily available to satisfy any judgment and that those assets are reachable by the State. The intervenors have made no demonstration to the contrary. The relief requested is, at bottom, a last resort effort to leverage the Division's proceeding to obtain an outcome not obtainable in any other forum absent a finding of liability.

Conclusion

The Division should approve the Joint Petition. The evidence demonstrates that: (i) the proposed asset sale will benefit Rhode Island ratepayers; and (ii) the proposed asset sale will not negatively impact Southern Union's ability to pay for the remediation of the Bay Street Area in Tiverton if legally obligated to do so. In fact, the evidence demonstrate that the proposed transaction will strengthen Southern Union's already strong financial health and that Southern Union will be able to satisfy any obligation to fund the remediation.

Accordingly, the Division should unconditionally approve the proposed transaction.

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[6] As counsel for the plaintiffs in the federal lawsuit relating to the Bay Street Area acknowledged at the intervention hearing, "[w]e are not concerned that we can't collect when we do get a judgment." (Hr. Tr. at 52.) Plaintiffs' counsel's confidence in the ability to collect a judgment from Southern Union not only belies the intervenors' purported concern that Southern Union will not have the financial wherewithal to satisfy a potential judgment but also demonstrates that requiring an escrow fund is both improper and unnecessary.

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Dated: July 11, 2006

CERTIFICATION

I hereby certify that I mailed a copy of the within to counsel of record, as set forth on the attached Certification List, via e-mail and first class mail on the 11th day of July, 2006.

Cynthia Lomas

National Grid & Southern Union - Docket D-06-13
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