THE STATE OF NEW HAMPSHIRE

BEFORE THE
PUBLIC UTILITIES COMMISSION

CITY OF NASHUA'S PETITION FOR VALUATION PURSUANT TO RSA 38:9

Docket No. DW04-048

CITY OF NASHUA'S MEMORANDUM OF LAW REGARDING (1) AUTHORITY TO TAKE ASSETS OUTSIDE MUNICIPAL BOUNDARIES UNDER RSA 38 AND (2) NASHUA'S VOTES UNDER RSA 38

The Commission's Order No. 24,379 dated October 1, 2004 called for briefs on (1) "whether RSA Chapter 38 provides Nashua authority to take PEU, PAC and the entirety of PWW," i.e., "assets of PWW that are not integral to the core system"; and (2) "whether Nashua has properly followed the voting requirements of RSA 38 and whether the votes taken are consistent with the requests made in the Petition." (Order, page 11).

RSA 38 allows the City of Nashua to take any Pennichuck plant and property required to promote the public interest as determined by the Commission.

RSA 38 links the scope of authority to take plant and property outside municipal boundaries to the scope of the public interest protected by the Commission. In four places, the statute makes clear that the Commission is intended to determine how much plant and property situated outside the municipality the public interest requires the municipality to acquire:

(1) RSA 38:2 I empowers a municipality to acquire plants for distribution of "water for municipal use, for the use of its inhabitants and others,

and for such other purposes as may be permitted, authorized or directed by the commission."

(2) RSA 38:6 provides for written municipal notice to the utility of plant and property it seeks to acquire including that "portion, if any lying without the municipality which the public interest may require, pursuant to RSA 38:11 as determined by the commission."

(3) RSA 38:9 I describes the issues that either party may present to the PUC, including "how much, if any, of the plant and property lying within or without the municipality the public interest requires the municipality to purchase."

(4) RSA 38:14 expressly sets certain conditions for a municipality's operation of "the plant, property, or facilities of a public utility in any other municipality," including the potential for the second municipality, in turn, to establish its own waterworks by eminent domain.

The "public interest" standard of RSA 38 does not limit extra-municipal acquisitions to property that is absolutely essential for water service within the municipality (e.g. reservoirs or wells for water supply). RSA 38:12 makes this clear. It permits a municipality with an existing plant (i.e., a fully functioning system) to expand beyond its boundaries pursuant to RSA 38:6-11 (i.e., by eminent domain). Consequently, an expansion of this sort is, by definition, beyond the scope of what is essential for service within the municipality.

RSA 38:11 also links the power to take to the breadth of public interest concerns. It provides that "[w]hen making a determination as to whether the purchase or taking of utility plant or property is in the public interest under this chapter, the Commission may

set conditions and issue orders to satisfy the public interest. . . . " In order to set such conditions and issue such orders, the Commission must have sufficient authority to do so, including the power to require/allow purchase of sufficient plant and property outside municipal boundaries to address any public interest issues that apply outside municipal boundaries.

In short, the statute indicates that the scope of authority to acquire extra-municipal plant and property is commensurate with the scope of the public interest that the Commission is authorized to consider.

The scope of "public interest" concerns under RSA 38

In public utilities theory and law, a state may use the police power to regulate businesses "affected with a public interest". 64 AmJur 2d Public Utilities, §15, p. 458. The term "public interest" denotes the various interests of consumers, investors, other interested parties and the general public that must be considered and balanced by a public utilities regulator in decision-making prescribed by statute. The New Hampshire Supreme Court has not construed RSA 38 "public interest," so other authorities may be referred to.

"Public interest" under other public utility statutes in New Hampshire

The focus of "public interest", or "public good," varies somewhat with the type of decision delegated to the Commission, but is typically broad. E.g.:

- RSA 369:1 and 4 require the Commission to approve issuance of securities for utility financing only upon a finding that the objects and amounts of the financing

will be in the "public good", i.e., "reasonable taking all interests into consideration" or "reasonably to be permitted under all the circumstances of the case". Appeal of Conservation Law Foundation, 127 N.H. 606, 614-15 (1986), citing earlier cases. The primary concern is ensuring acceptable service at reasonable rates. Id. at 615.

- RSA 374:26 requires a finding of "public good" and "public interest" for granting of a new or extended public utility franchise. The respective advantages and disadvantages of ratepayers within and without the area in question must be balanced. Parker-Young, Co. v. State, 83 N.H. 551, 563 (1929).
- RSA 374:30 requires a finding of "public good" for a transfer of control of utility facilities. The general welfare of the utility itself may predominate, for example, where insolvency is threatened. Appeal of Legislative Utility Consumers' Council, 120 N.H. 173, 174 (1980).
- RSA 375-B:7 calls for any permit issued to a contract carrier to be in the "public interest", defined broadly to include the needs of the public at large as well as the utility and other particular persons directly affected. Browning-Ferris Indus. v. Public Util. Comm'n., 116 N.H. 261, 262 (1976).
- RSA 378:27 & 28, of course, call for public utility rates to be in the "public interest", delegating to the Commission "the difficult task of deciding among many competing arguments and policies in reaching decisions that serve the public interest". LUCC v. Public Serv. Co. of N.H., 119 N.H. 332, 339 (1979).

RSA 38 "public interest" in Commission decisions

The meaning and scope of "public interest" under RSA 38 has been addressed in decisions of the Commission:

- In Petition for Valuation of J. Brodie Smith Hydro-Electric Station, DE-00-211, Order No. 24,086, the city sought to acquire hydro-generating facilities from PSNH. The Commission posed the public interest question as a balancing of public goods and public harms. The factors presented for the Commission were the statutory presumption created by the favorable city referendum vote; the city's projected reliable supply of reasonably priced electricity; the adverse impacts on the PSNH ratepayers outside Berlin; and the effects on the PSNH workers whose jobs were likely to be affected.
- In Petition of Town of Ashland, DE-03-155, Order No. 24,214, the town sought to acquire plant and property of NH Electric Cooperative to serve Ashland residents. Arguing that the "public interest" test was a "no net harm" standard, the town claimed that rates would be lowered for the Ashland customers, while the Cooperative pointed to the adverse cost-shifting to other Cooperative ratepayers elsewhere in its system.

"Public interest" in water company eminent domain in other states

Appellate court decisions in municipal waterworks acquisition cases in other jurisdictions have discussed the scope of public interest:

- In City of Missoula v. Mountain Water Co., 228 Mont. 404, 743 P.2d 590 (1987), the city sought to acquire a water system that served customers both inside and

outside the municipal boundaries. (Under Montana statute, the "public interest" test required a finding that the taking be a "more necessary" public use than utility ownership, a stricter standard than RSA 38. Id. at 411-12.)

The court found relevant to "public interest" all the following factors: (a) the impact on water company employees; (b) effects of company profits and out-of-state ownership; (c) savings on rates and charges; (d) the level of cooperation between the water company and the city; (e) the "public interest" expressed in the city council and referendum votes; (f) the importance of city control of water rights to assure long-range access to water supply. Id. at 413-14.

- In Middletown Twp. v. Pa. P.U.C., 85 Pa. Commw. 191, 482 A.2d 674 (1984), the water company operated an integrated water supply and distribution system serving customers in three municipalities. The township sought to acquire only the system's facilities within the township. The Pennsylvania P.U.C. found that the acquisition would benefit most customers in the township but would have an adverse effect on commercial customers in the township and customers in the other communities, and therefore denied the acquisition as not in the public interest. Id. at 197. The court upheld the decision, emphasizing that the "public interest" measures the benefits and detriments of the acquisition on all affected parties. Id. at 202-03.

The scope of "public interest" in the present case

As illustrated above, determination of "public interest" is certainly concerned with impacts on rates and quality of service to both customers of the waterworks facilities being acquired and residual customers of the privately owned portions of the system. The importance of the local votes must also be considered. Analysis is also apt to consider the impacts on water company employees and long-term local control of water supply and protection areas.

In the present case, the City seeks to acquire all the assets of the three Pennichuck regulated utilities because the City believes it would promote the interests of all customers/ratepayers, the general public, the employees of Pennichuck and, indeed, the owners of Pennichuck. The will of Nashua voters would be implemented; the goals of the Merrimack Valley Regional Water District, organized under Laws 2003, Chapter 281, would be promoted; rates would be lower over time; service would remain adequate; water supplies would come under long range public control; continued employment of Pennichuck operation and maintenance personnel would be reasonably accommodated; and Pennichuck owners would receive fair value for their assets without the disadvantages of retaining ownership of smaller systems only.

The present case, however, differs from efforts to municipalize water or electric public utilities cited above in one important respect. In the other cases, a portion of a single water or electric system was proposed for municipalization. In the present case, as Pennichuck points out in its Motion To Dismiss (paragraph 5), "PEU, PAC, and PWW are separate legal entities, each with its own assets, its own service territories and its own corporate and legal history. On the other hand the Pennichuck operations are

somewhat integrated. PWW has historically supplied employees, office facilities, and office equipment to Pennichuck Corporation, PEU, and PAC for a fee. See management fee agreement dated January 1, 2001 on file with the Commission (copy attached as Exhibit A, furnished in response to City's Data Request No. 1-11 in Case No. DW 04-056). Perhaps similar arrangements exist for operations and maintenance personnel and equipment working in the field. If only certain PWW facilities were acquired by Nashua, arguably there would be losses of economies of scale to residual water utility operations with resulting impacts on cost and quality of service. Given the issue of the extent of taking authority under RSA 38, a key question is whether such indirect impacts on separate water systems would be factored in to the determination of "public interest", or be outside the Commission's area of concern under RSA 38.

In other jurisdictions, the issue has arisen in the context of whether a municipality must pay severance damages for such incidental losses when acquiring a portion of a water company's multiple systems. The leading case is Kennebec Water Dist. v. City of Waterville, et al., 97 Me. 185, 54 A. 6 (1902). The water company claimed severance damages for the proportionally heavier costs of supervision and management to its remaining property attributable to the loss of its Waterville plant. The court summarized the circumstances:

> The compensation asked is not for property taken, but for incidental damages to other property having no physical connection with or contiguity to that taken, and having no relations whatsoever with the property taken, except those which grow out of common ownership.

54 A. at 17. Applying general eminent domain principles, the court held that no severance damages could be awarded because the properties were separate and distinct, and the damages were incidental and consequential. Id. at 17-18. The

Kennebec Water District holding was subsequently reaffirmed in East Boothbay Water Dist. v. Boothbay Hbr., 158 Me. 32, 41, 177 A.2d 659 (1962). The same result was reached in South Bay Irr. Dist. v. Calif. – American Water Co., 61 Cal. App. 3d 944, 133 Cal. Rptr. 166 (1976), where the water company owned two water supply and distribution systems that were physically separate and were separate enterprises for rate-making purposes. The two systems jointly used office and operations facilities. The facilities were included in the rate base of the system condemned by the municipality. The water company sought severance damages for the cost the second system would incur to replace the facilities. The court ruled that the facilities were part of the first system, and no severance could be awarded for separate systems. All compensable value must be found in the facilities themselves. 61 Cal. App. 3d at 1002-03.

If the Commission is inclined to take an expansive view of the "public interest" under RSA 38 to include indirect effects on PEU and PAC, then it is essential to also interpret the scope of Nashua's potential authorized taking expansively. City acquisition of PAC and PEU and non-core PWW could eliminate loss of economies of scale and prevent severance damages. A scope of taking commensurate with the scope of "public interest" protection is required to fulfill the purpose of RSA 38, to allow the Commission to balance all relevant factors and to issue orders and attach conditions under RSA 38:11 to produce the optimal outcome.

Legislative History of RSA 38

The history of RSA 38 establishing the ability of a municipality to acquire property outside its boundaries is unbroken. Beginning with the passage of Laws 1913, Chapter 218:2-5, which became Public Laws, Chapter 44 the Legislature incorporated the concept of a municipality purchasing electric plant and property outside its limits. "Where the major part of the plant, property or facilities of such utilities lies within the limits of the municipality" and the public service commission, the predecessor of the PUC, determines the purchase "is for the public interest and necessary for the proper carrying on of its business", "taking into consideration the rights of the public utility and of the other municipalities in which it operates", a municipality may purchase the whole or part of the plant or property outside its limits. (emphasis supplied) PL 44:13. A copy of PL 44:13 is attached as Exhibit L.

This concept of acquiring property outside a municipality if it is in the public interest has been utilized by the Legislature from the outset, and subsequent amendments and re-enactments have done nothing to diminish it.

In Laws 1935, Chapter 153, which substituted a new Chapter 44, Section 5 (Demand) was amended to permit acquisition of the plant and property lying outside the municipality "which the public interest may require the said municipality to purchase." Exhibit M. Likewise, Section 8 (Valuation) introduced the principle of the municipality acquiring property lying outside the municipality, which the public interest requires. Exhibit M. Since Section 8 permitted the utility to likewise petition the commission to make such a determination, it is apparent that the Legislature envisioned instances in which the utility would want the municipality to acquire its property outside the

municipality's limits such as when the utility would be left with small, uneconomic portions of its business.

These concepts have continued unchanged into the current RSA 38 as is apparent from the testimony of Rep. Clifton Below on April 21, 1997 before the Senate Committee on Executive Departments and Administration regarding House Bill 528, which was enacted as Laws 1997, Chapter 206 and codified as the current RSA 38. In discussing the ability of the PUC to set conditions and issue orders to satisfy the public interest under RSA 38:11, Rep. Below said:

> This clarified their ability to positively assert conditions or even issue orders that say the public interest requires, for instance, that a municipality may have to acquire some property outside of its boundaries. If there is some customers that would otherwise be stranded with a small distribution line that crosses a municipal boundary the commission would have the power to order the utility that is selling its property or having its property acquired and also order the municipality to acquire that portion of a system that may be outside of their boundaries.

The extent to which the Legislature viewed the public interest determination to be broad is evident from Rep. Below's testimony regarding valuation.

> There was some question about the whole valuation process. There was consideration to whether it should be thrown to the board of tax and land appeals in terms of the appeal procedure to the commission determination. It was felt that the commission in many ways really was more expert in terms of utility property and in terms of how it was going to balance the public interests between shifting costs to say an existing rate base versus a municipalized effort, i.e., if you set the price too low in an acquisition, you would actually potentially shift cost onto existing ratepayers that are left behind with the incumbent utility.

There is nothing in the legislative history which would indicate an intent on the part of the Legislature to preclude a municipality from taking utility property outside its boundaries. Rather, the history is clear that not only were such acquisitions permitted,

they might even be required, in the public interest. The public interest determination has been made paramount.

PEU and PWW have argued that RSA 38 does not extend to takings from a utility that does not provide service within the municipalities' boundaries. RSA 38:6. Such an argument is not supported by the broad public interest determination envisioned by the Legislature and apparent from the legislative history. In giving the PUC the power to require the purchase of property outside the municipality's boundaries if it is in the public interest, the Legislature recognized that there might be situations, such as here, where property, which is part of a utility system and lying outside the municipality, if not acquired would result in a shifting of cost to the remaining ratepayers. See testimony of Rep. Clifton Below, supra. Its solution was to permit and perhaps even to require the property to be acquired to prevent such a result. The argument of PEU and PAC would prevent the PUC from making this kind of broad public interest determination, which the statute so clearly contemplates.

Moreover, the argument ignores the reality of the relationship among PWW, PEU and PAC. While they are separate corporations, they were created that way for rate purposes and are subsidiaries of a single utility holding company. They are a part of a "system" as described by Rep. Below, in the broad sense of being linked by economies of scale. It makes sense for an acquirer of the assets of one of the companies to own the assets of all three and that is what the City seeks in its Petition.

Voting Requirements of RSA 38

RSA 38 contains a road map for municipalities to follow to acquire, as here, a suitable plant for the ”manufacture and distribution” of “water for municipal use, for the use of its inhabitants and others and for such other purposes as may be permitted, authorized, or directed by the commission”. (Emphasis supplied) RSA 38:2(I). A city, such as Nashua, may establish a plant “after 2/3 of the members of the governing body shall have voted subject to the veto power of the mayor as provided by law, that it is expedient to do so, and after such action by the city council shall have been confirmed by a majority of the qualified voters at a regular election or at a special meeting duly warned in either case”. RSA 38:3.

On November 26, 2002, the Nashua Board of Aldermen, pursuant to RSA 38:3, by a vote of 14-1, determined that it was “expedient for the city to establish a water works system and, in order to establish such water works system, to acquire all or a portion of the water works system currently serving the inhabitants of the City and others.” (Emphasis supplied) Exhibit B.

The language of the Resolution, drafted by the City’s attorneys and bond counsel, Palmer & Dodge of Boston, MA, follows the language of RSA 38:2 and 3 and clearly intends the acquisition of a system which serves not only the inhabitants of Nashua but also “others”. The Aldermen’s intent to seek to acquire assets outside Nashua for the purpose of establishing a regional water district is further evident from the findings it made in connection with the Resolution. Exhibit B.

On November 26, 2002, the Alderman also voted to hold a special election on January 14, 2003 to seek the confirmation of its action by a majority of City voters

pursuant to RSA 38:3. The question to be presented to the voters, again drafted by the City attorneys and Palmer & Dodge, with knowledge of the Aldermen's intent to seek to acquire assets outside Nashua, was:

> Shall the resolution of the Board of Alderman adopted on November 26, 2002 determining that it is expedient for the City to establish a water works system and in order to establish such water works system, to acquire all or a portion of the water works system currently serving the inhabitants of the City <u>and others</u> be confirmed?" (Emphasis supplied)

The procedure followed by Nashua is the procedure required by RSA 38 and is the same as that followed by the City of Berlin in its earlier attempt to acquire the J. Brodie Smith Hydro-Electric Station from PSNH (DE 00-211). Berlin initially sought the acquisition under the provisions of Laws 2000, Ch. 249:5 but then took the requisite RSA 38:3 vote of the qualified voters of the City. Following the vote, Berlin elected to proceed under Chapter 38 rather than Laws 2000, Ch. 249:5. The Commission agreed that Berlin, having taken the required vote, was entitled to proceed under RSA 38 over the objection of PSNH (DE 00-211; Order No. 23,775, Sept. 7, 2001).

Following the adoption of the November 26, 2002 Resolution, the Aldermen conducted public hearings and meetings in all of the wards of Nashua during which the proposed acquisition, including property outside Nashua and the regionalization efforts, was discussed. Attached as Exhibits C - I are copies of articles appearing in the Nashua Telegraph on June 6, 2003, January 7, 2003, January 8, 2003, January 10, 2003, January 11, 2003, January 12, 2003 and January 14, 2003, respectively. These articles report not only the extensive effort made by the City through the meetings in the wards and other forums to inform the voters about its intended acquisition but also document the fullness of the debate. Pennichuck Corp., the parent of PWW, PEU and

PAC, engaged in a vigorous public relations campaign to defeat the resolution. What is apparent from all of these articles and the debate they report is the intent of the City to acquire property outside Nashua, including the assets of PEU and PAC. For example in the January 8, 2003 article, Exhibit E, it is reported that the merger price was approximately $95 million and that the company's advertisement says the City can't afford to spend $100 million to buy it. That even Pennichuck was aware of the City's intent is particularly evident from Exhibit F where a company official discusses what the City would have to pay over and above the merger price to make shareholders whole. Perhaps the most revealing article concerning Pennichuck's awareness of the City's intent to acquire the assets of PWW, PEU and PAC, including those outside Nashua was published on November 28, 2002, immediately following the adoption of the Resolution by the Alderman. (Exhibit J) In the article, Pennichuck's President and CEO Maurice Ariel is clear that the Company will require a sale of all of its assets to replicate the merger and that the price will have to be superior to the merger price. Any suggestion by PWW, PEU, PAC or any intervener that voters were not aware of the City's intent to acquire assets outside Nashua, including the assets of PEU and PAC borders on being disingenuous.

On January 14, 2003 by a 78% majority (6505 in favor, 1867 opposed), the voters of Nashua confirmed the Resolution of the Alderman, creating a rebuttable presumption that the acquisition is in the public interest, RSA 38:3.

Following the overwhelming confirmatory vote, the Alderman pursuant to RSA 38:6 determined that all of the property of PWW, PEU and PAC was necessary for its municipal utility service (Exhibit K) and on February 5, 2003 gave notice to PWW, PEU

and PAC of the vote and made inquiry whether they would sell the property it had identified. (Exhibits B, C and D to the Petition) The property identified is specific and comprehensive for all three companies.

It is apparent under RSA 38 that the governing body (in Nashua the Board of Aldermen) is responsible for the determination of the property to be acquired while the voters merely confirm the general determination that it is expedient to establish a water works system. Cf RSA 38:3 and RSA 38:6. RSA 38:12 makes this distinction between the roles of the Aldermen and the voters clear. Under RSA 38:12, a municipality, which has an existing plant can expand "in the manner prescribed by RSA 38:6-11". Even though such an expansion could include property outside the municipality there is no requirement to obtain a confirmatory vote under RSA 38:3. Having confirmed the general proposition that it is expedient to establish a municipal plant, the voters leave the specific determinations about what property to acquire and where to the governing body. Consequently, even though the Aldermen in Nashua were very clear with the voters about their intent to acquire property outside Nashua, there is no requirement for the City voters to do anything other than confirm the action of the Aldermen that it was expedient to establish a water works system and in order to do so to acquire all or a portion of the water works system currently serving the inhabitants of Nashua and others, which they did. Any argument that the January 14, 2003 vote was not adequate fails to comprehend the different roles given to the Aldermen and voters under RSA 38.

Conclusion

RSA 38 supported by its legislative history provides the City of Nashua authority to take the assets of PWW, that are not integrated to the core system, located outside

Nashua, as well as the assets of PEU and PAC, if that is determined to be in the public interest by the Commission. Moreover, the City has properly followed the voting requirements of RSA 38 and all votes taken pursuant to the statute are consistent with the City's Petition to acquire the assets of PWW, PEU and PAC.

Respectfully submitted,

CITY OF NASHUA

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Dated: October ___, 2004

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CERTIFICATION

I hereby certify that a copy of the foregoing Pleading was this day forwarded to all persons on the attached Service List.

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Robert Upton, II