

DW 01-215

HAMPTON WATER WORKS, INC.

Joint Petition for Approval for a Change of Control

Order Approving Petition

O R D E R N O. 23,924

March 1, 2002

APPEARANCES: Ransmeier & Spellman by Dom S. D'Ambruoso, Esq. for Joint Petitioners Aquarion Company, Hampton Water Works Company, American Water Works Company, Inc. and Greenwich Water Systems, Inc; Office of the Consumer Advocate by Kenneth Traum; Shaines & McEachern by Peter Doyle, Esq. for intervenor Town of Hampton; and Marcia A. B. Thunberg, Esq., on behalf of Staff of the New Hampshire Public Utilities Commission.

I. PROCEDURAL HISTORY AND BACKGROUND

On October 31, 2001, Aquarion Company (Aquarion), Hampton Water Works Company (Hampton), American Water Works Company, Inc. (AWWC) and Greenwich Water Systems, Inc. (GWS), (collectively, "Petitioners"), filed with the New Hampshire Public Utilities Commission ("Commission") a Joint Petition for approval for a change of control of Hampton Water Works Company.

The Petitioners requested Commission approval of Aquarion's purchase of all outstanding common and preferred stock of Hampton owned by AWWC and GWS. Hampton is a wholly-owned subsidiary of GWS, and GWS is a wholly-owned subsidiary of AWWC. The Petitioners also requested that Aquarion be permitted to exercise control over Hampton and operate Hampton according to the

representations made in the Petition.

On January 4, 2002, Petitioners filed an amendment to their Petition which requests, in addition to the terms set forth in the original Petition, that promptly on the closing of the transaction, Aquarion be permitted to transfer all of the outstanding common and preferred stock of Hampton then owned by Aquarion to Aquarion's new intermediate holding company subsidiary, Aquarion Water Company, and to change the name of Hampton to "Aquarion Water Company of New Hampshire."

Aquarion, AWWC and GWS represent that the acquisition described in the Petition will have no adverse effect on rates, terms, conditions or operations of Hampton. Also, they assert that jurisdiction of the Commission over Hampton's current operations will not be changed and the transaction will have no impact on Commission orders pertaining to Hampton.

The Commission issued an Order of Notice establishing a pre-hearing conference and technical session for December 20, 2001 and requiring public notice. On December 5, 2001, the Town of Hampton filed a motion to intervene. On December 14, 2001, the OCA filed a notice of intent to participate in the docket on behalf of residential utility customers. On January 17, 2002, pursuant to Commission Order No. 23,902, the Commission approved a procedural schedule and granted the Town of Hampton's intervention. The parties

conducted a technical session on December 22, 2001, a settlement conference and another technical conference on January 25, 2002. The parties also engaged in discovery and exchanged numerous data requests and responses. As a result of the discussions and discovery, the parties reached agreement on several issues and filed a Stipulation regarding same on February 5, 2002. A hearing on the Stipulation was held on February 8, 2002.

II. POSITIONS OF THE PARTIES AND STAFF

A. Petitioners

The Petitioners summarized the elements of the Stipulation through their witness, Janet M. Hansen, Executive Vice President of Aquarion. The elements of the Stipulation are further stated later in this order. Witness Peter Galant of BHC Company, an Aquarion subsidiary, also provided testimony concerning the level of capital investment in infrastructure that is expected to be made in the coming years. The Joint Petitioners requested the Commission grant their Joint Petition expeditiously.

B. Town of Hampton

The Town of Hampton expressed its support for the Stipulation.

C. Office of the Consumer Advocate

The OCA stated that through its participation in the docket that it had overcome its initial opposition to this merger.

OCA signed the Stipulation and wholeheartedly supports the transaction. OCA believes that based upon the commitments contained in the Stipulation and commitments expressed in data responses, the Petitioners' proposed change of control of the utility will not harm residential ratepayers. OCA believes that the issues of management decision-making and local input have been adequately addressed. OCA expressed its view that Aquarion is a good company. OCA specifically supported paragraphs 5 and 6 of the Stipulation relating to acquisition costs and merger savings. These paragraphs allay OCA's concerns about enabling a company to recover acquisition costs and the problem of proof against a hypothetical. OCA asserted that under traditional ratemaking, paragraph 6, Merger Savings, the Commission should only enable the company to recover the actual dollars spent. OCA stated some precedent exists in New Hampshire for an incentive on the return on equity but that issue should wait for a traditional ratemaking proceeding.

D. Staff

Staff supported the Stipulation and also urged the Commission approve the Petitioner's Petition.

III. SUMMARY OF STIPULATION

The Stipulation was signed by Aquarion Company, Hampton Water Works Company, the Town of Hampton, the Office of the Consumer Advocate, and Staff of the Commission and was submitted for

Commission review on February 5, 2002. The elements of the Stipulation are summarized as follows:

A. Public Interest Standard

The Parties and Staff agree the proposed acquisition of HWWC by Aquarion met the public interest standard of RSA 374:33, and, as required by RSA 369:8, II, it will have no adverse effect on HWWC's rates, terms, conditions, or operations of HWWC.

B. Fitness Standard

The Parties and Staff agree Aquarion has the legal, managerial, financial, and operational expertise to operate HWWC in a manner that will have no adverse impact on HWWC and its customers.

C. Jurisdiction

The Parties and Staff agree the transaction will not change the Commission's authority as to HWWC.

D. Compliance

Aquarion commits it will operate HWWC in accordance with New Hampshire law and in accordance with HWWC's existing tariffs.

E. Acquisition Costs

Aquarion commits it will not pass, either directly or indirectly, any acquisitions costs or premiums onto customers of HWWC, in this docket or any future proceeding.

F. Merger Savings

Aquarion reserves the right, at the time of future rate cases, to request an opportunity to make a showing that Aquarion's acquisition of HWWC has resulted in savings and benefits to HWWC customers. The Parties agree the Commission may consider reflecting this superior performance through an increment to the otherwise determined market based rate of return. Aquarion commits that it will not file for a general rate increase for HWWC during year 2002.

G. Change of Name

The Parties and Staff agree HWWC will be named Aquarion Water Company of New Hampshire, contingent upon final approval of the name from the NH Secretary of State. Aquarion commits that it will not charge HWWC customers for any costs associated with the name change.

H. Service Agreement

Aquarion intends to enter into a new service agreement, submitted as a response to OCA data request Set 1, #3 and Staff data request Set 1, #2-8, with the former HWWC relating to the provision of support services such as billing, accounting, public affairs, customer service, and meter repair.

I. Customer Billing

Aquarion will replace HWWC's existing bill form with a common bill form to be used by all Aquarion utility billings. Prior to making such changes, Aquarion will seek input from the Town and the

Commission's Consumer Affairs Division.

J. Source of Supply/Conservation

Aquarion commits to continue to identify and develop new sources of supply and to eliminate the current moratorium on new connections. Aquarion also commits to implement a conservation program which will include an education component for middle school-aged children.

K. Water Quality/Operations

Aquarion commits to maintaining water quality which meets all federal and state standards. Aquarion commits to maintain and enhance HWWC's customer service, research and development, information technology, and replacement of aging infrastructure.

L. Local Relationships/Collective Bargaining Agreement

Aquarion commits to assuming the obligations fo the existing collective bargaining agreement between HWWC and the United Steelworkers of America, AFL-CIO-CLC. Aquarion commits to assuming obligations of pension payments. Aquarion commits to maintaining the local relationship HWWC had established with the community. Further, Aquarion commits to maintaining the current advisory board.

M. Financing

Aquarion commits to utilizing the least cost financing and, when available, tax exempt financing for HWWC capital additions.

IV. COMMISSION ANALYSIS

A. Scope of Review

The Commission stated in the Order of Notice that this transaction raised, inter alia, issues related to: RSA 369:8 and corporate mergers and acquisitions; 374:4 regarding Commission oversight of the management of utility operations as well as the safety, adequacy and accommodation of the utility service provided; RSA 374:30 relative to authority of public utilities to transfer or lease franchises, works, or systems when the Commission finds it in the public good; and RSA 374:33 relative to acquisitions being lawful, proper and in the public interest.

As the Commission previously held in Order No. 23,308, *New England Electric System*, 84 NH PUC 502 and Order No. 23,470, *Energy North Natural Gas, Inc.*, 85 NH PUC 361 (2000), a petitioner's representations that no adverse effect on the rates, terms, service or operation of the utility will occur, though a facial satisfaction of RSA 369:8, II, is not enough to warrant approval of a merger transaction. Although RSA 369:8, II (a) and (b) may appear to allow an exemption regulatory scrutiny if a Petitioner files the requisite statement 60 days prior to the transaction, we believe this provision

must be viewed in the context of the Commission's overall statutory mandate. This is consistent with the tenet of statutory construction that the intent of the legislature as expressed in the words of a statute are considered as a whole. See *State v. Duquette*, 145 NH 374, 376 (2000).

The Commission is explicitly granted investigatory powers under RSA 365:5. We are required to assure rates are just and reasonable, and we must assure the citizens of this state that transactions such as the one at issue here are lawful, proper and in the public interest. Additionally, we are vested with a specific duty to "keep informed" as to the operation of all public utilities in the state, RSA 374:4, and are empowered to "investigate or make inquiry . . . as to any act or thing having been done, or having been omitted or proposed by any public utility," RSA 365:5 (emphasis added). Further, pursuant to RSA 374:30, a public utility may transfer its franchise, works or system when the Commission finds that "it will be for the public good."

In the context of the instant transaction, we conclude we are vested with both the power and the obligation to conduct an inquiry to verify the representations made by the Petitioners. As we have discussed in our previous decisions involving mergers or acquisitions of public utilities, this inquiry is guided by the directive in RSA 369:8, II that the transaction "will not adversely

affect the rates, terms, service, or operation of the public utility within the state" and the requirement in RSA 374:33 that the result is "lawful, proper and in the public interest."

B. Effect on Rates

Aquarion has committed to not file for a rate increase until after 2002. Aquarion plans to spend approximately one year consolidating HWWC into its structure and operations. Aquarion has also agreed not to seek recovery of acquisition costs or costs associated with the name change of Hampton Water Works Company to Aquarion Water Company of New Hampshire. (As an aside, we note the name change must be approved by the New Hampshire Secretary of State and such approval had not been obtained as of the time of the hearing.) We believe these commitments to limit charges passed along to customers in general aid in rate stability and are tangible benefits to the customers.

C. Customer Service/Local Character

At the public hearing held January 24, 2002, area residents repeated concerns that the local connections they had developed with HWWC be preserved. The residents obviously valued the company in the community. Further evidencing the company's ties to the community were specific references to employees Mr. Bossum and Mr. Goetz and their involvement in local issues. Other residents expressed concern for company retirees living in the area and the

security of their company pensions. The plight of the area aquifer and HWWC's support of water conservation efforts was mentioned, as were rate stability and customer service issues. In short, residents clearly want assurance Aquarion will fill the shoes of this respected local company.

Aquarion's witness, Ms. Janet Hansen, testified that the company had a strong commitment to its customers and that the customers will see no change in the way they interact with Hampton Water Works on a local basis. (Transcript at 35). Backing up the assertion, the Stipulation states at paragraph 17, Local Relationship, that Aquarion will maintain a level of staffing in its local office that is sufficient to provide across the counter service to customers and to respond to customer calls and correspondence that are directed to the local office rather than Monroe, Connecticut. Aquarion also commits to maintain local operations such that quality of service will be of the highest priority and that customer service currently provided will not be adversely impacted. Aquarion has also committed in paragraph 16 of the Stipulation to using the existing Hampton Water Works Company Advisory Board. (See also Hearing Transcript at 22.) This mechanism should help ensure that New Hampshire customer's voices are heard by the parent company.

We are satisfied with the representations of Aquarion that the transaction will not have a negative effect on the local operation and character of the HWWC. We will continue, however, to monitor operations and customer service carefully and hold the new management to its commitments. Thus, our determination here is expressly based upon our expectation of adherence to the commitments contained in the Stipulation.

D. Acquisition Premium/Merger Savings

In *Northern Utilities, Inc.*, 83 NH PUC 401 (1998), we noted that the inclusion of an acquisition premium in the revenue requirement calculation, and the effect of the acquisition premium on capital structure, would in all likelihood lead us to the conclusion that customers would be harmed by the acquisition.

In other transactions we have held that even under the "no net harm" test we could, in principle, warrant conditioning our approval of the transaction on a prohibition against recouping acquisition costs. See *New England Electric System*, 84 NH PUC 502, 512 (1999).

Paragraph 5, Acquisition Costs, of the Stipulation contains a commitment from Aquarion that no costs, including acquisition costs and premiums paid by Aquarion, HWWC, or American related to this transaction shall be borne by customers. We will approve the agreement between the Parties and Staff to the effect

that Aquarion will be barred from recovery of any acquisition premium. Thus, any merger related costs shall be recorded and amortized "below the line" and shall not be included in the determination of rates in this or future proceedings.

Paragraph 6 of the Stipulation defers consideration of the merger savings for a subsequent proceeding. Because a rate case is likely to be filed within a reasonably short period of time, we accept this condition. The Stipulation further provides that if Aquarion makes a successful demonstration of savings that the Commission may consider reflecting this superior performance through an increment to the otherwise determined rate of return. The Stipulation does not bind any Party to any particular position and Parties are free to take any position they deem appropriate. We note that recovery of excess returns in light of merger savings may be interpreted as a form of recovery of the acquisition premium, and thus barred under ordinary ratemaking principles.

V. CONCLUSION

Mergers of a very small company into a larger company may result in customers benefitting from the expertise and access to capital markets which are generally available to the larger entity, with its greater financial and other resources. Aquarion witness Janet Hansen testified Aquarion was backed by Kelda, a large British

company that pursues innovation in water works technology, but does not interfere in local management issues. (Hearing Transcript at 8). Ms. Hansen also testified to the strong track record in Connecticut of Aquarion's subsidiary, BHC Company. She stated that this record demonstrated Aquarion has the legal, managerial, financial, and operational expertise to operate Hampton Water Works. Also, Ms. Hansen testified that this background and state-of-the-art technology from Kelda will enhance Hampton Water Works' operations and community involvement. (Hearing Transcript at 9 and 10). These are among a number of synergies this Commission finds beneficial to the public from this proposed acquisition.

After careful review of the Stipulation, testimony, exhibits, and comments offered at the January 24, 2002 public hearing, and based upon the foregoing analysis, the Commission concludes the acquisition of Hampton Water Works Company by Aquarion will produce net benefits for HWWC customers. We therefore approve the transaction. We do so with the understanding that Aquarion will abide by the commitments made in the Stipulation and Data Responses, which were incorporated by reference into the Stipulation.

Based on the foregoing, it is hereby

ORDERED, that the acquisition of Hampton Water Works Company by Aquarion, will have no adverse effect on the rates, terms, service or operation of the company within the State and will be in the public good and for the public interest, consistent with the requirements of RSA 369:8, II and RSA 374:33, provided all of the terms and conditions of the Stipulation, incorporated herein, and this Order are met, and is therefore APPROVED; and it is

FURTHER ORDERED, that the authority granted to Aquarion to acquire Hampton Water Works Company shall be exercised within one year from the date of this Order, and shall not be exercised thereafter without further order of the Commission, and it is

FURTHER ORDERED, that Hampton Water Works Company shall surrender its certification in New Hampshire by filing a supplement canceling their existing tariff; and it is

FURTHER ORDERED, that the Aquarion shall file a compliance tariff with the Commission in accordance with N.H. Admin. Rules, Puc 1603.02(b).

By order of the Public Utilities Commission of New
Hampshire this first day of March, 2002.

Thomas B. Getz
Chairman

Susan S. Geiger
Commissioner

Nancy Brockway
Commissioner

Attested by:

Debra A. Howland
Executive Director and Secretary