

STATE OF NEW HAMPSHIRE
SUPREME COURT

2009 Term

Case # 2009-0274

Appeal of City of Nashua;
Appeal of Pennichuck Water Works, Inc. & a.

BRIEF OF ANHEUSER-BUSCH

John T. Alexander
Daniel J. Mullen

Ransmeier & Spellman, P.C.
One Capitol Street
P.O. Box 600
Concord, N.H. 03302

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STATEMENT OF THE CASE

In March 2004 the City of Nashua filed a petition with the New Hampshire Public Utilities Commission (the “Commission” or “PUC”) seeking to acquire Pennichuck Water Works (“PWW”) and its affiliates Pennichuck East Utilities (“PEU”) and Pittsfield Aqueduct, Inc. (“PAC”) pursuant to RSA 38:9. As PWW’s largest customer, Anheuser-Busch, Incorporated (“AB”) intervened. On January 21, 2005 the Commission issued an order allowing the action to go forward with respect to PWW, but dismissing the action with respect to PEU and PAC. The Commission conducted hearings on the merits in January and September 2007.

On July 25, 2008 the Commission issued an order approving Nashua’s petition, finding that PWW had failed to rebut the presumption under RSA 38:3 that the acquisition of PWW’s plant and property is in the public interest. The Commission also authorized Nashua to acquire the assets of twenty-one community water systems outside of Nashua owned and operated by PWW. The Commission valued the property to be taken at \$203,000,000 as of December 31, 2008. The Commission set several conditions on the acquisition, including the establishment of a mitigation fund of \$40,000,000 to protect customers of PEU and PAC. On March 13, 2009 the Commission denied both parties’ motions for reconsideration.

PWW now appeals the determination that the acquisition is in the public interest. It also challenges the constitutionality of RSA 38, the Commission’s application of that statute, and the imposition of conditions to bring Nashua’s proposal within the public interest. Nashua appeals the dismissal of its action with respect to PEU and PAC, and the determination of the fair market value of PWW’s assets. The Merrimack Valley Regional Water District has also submitted a brief supporting Nashua’s position on valuation.

STATEMENT OF FACTS

Anheuser-Busch operates a brewery in Merrimack that employs more than 400 people. In 1970, AB and Pennichuck Water Works collaborated in a main extension from PWW's core system in Nashua to AB's facility. Day XI, p. 45. A number of other businesses in Merrimack have since tied in to that main extension. Day II, p. 72. PWW has supplied AB with water pursuant to a series of long-term special contracts. AB uses this water to produce its beer, as well as for other plant purposes. AB is PWW's largest customer, accounting for more than ten percent of the system's average daily volume of water sales. AB has four principal requirements for its water supply: (1) high-quality water; (2) reliable service; (3) long-term, stable rates that are reasonable and cost-based; and (4) operational cooperation with its supplier.

PWW has consistently met each of these requirements. The special contracts have permitted AB to make long-term decisions for its Merrimack facility by providing stable, cost-based rates for water. The contracts have also benefited PWW by assuring a reliable, high volume of sales with minimal operational complications and costs, keeping rates lower for PWW's other customers. Oversight by the New Hampshire Public Utilities Commission has been invaluable in helping AB and PWW reach and implement their agreements and maintain good working relations.

The current supply contract is effective from July 1, 2005 to July 1, 2015. Anheuser-Busch pays a cost-based rate approved by the Commission in accordance with a cost of service study. The Commission has found that "service to AB constitutes a special circumstance because of its high level of consumption and the low level of cost associated with providing that service," that the special circumstance justifies departure from PWW's general rate schedules,

and that the departure described in the AB supply contract is “just and reasonable, and consistent with the public good in accordance with RSA 378:18.”

The current special contract states that water supply is a vital element of Anheuser-Busch’s business, and that Anheuser-Busch relies on the contract in making long-term decisions about its acquisition of water and its operations in Merrimack as a whole. The contract provides that if a governmental entity acquires PWW’s facilities, that governmental entity shall assume PWW’s obligations to the fullest extent permitted by law. It further provides that insofar as legally possible, the benefits and burdens of the contract shall be binding upon the parties’ successors. Thus PWW and AB entered into the contract with the intention that a governmental entity taking PWW’s system by eminent domain would continue to honor the contract’s terms. In approving the contract, the Commission acknowledged the reasonableness of the provisions for transfer of the contract’s obligations to an acquiring governmental entity.

SUMMARY OF THE ARGUMENT

Anheuser-Busch is satisfied with the service PWW has provided for nearly forty years. The hearing evidence showed that PWW is a well-run company that has made commendable efforts to promote the interests of New Hampshire's citizens inside and outside of Nashua. AB does not doubt that the City and Veolia could also provide excellent water service. However, AB must base decisions about capital investment, plant expansion, and allocation of resources on the predictability of future operating costs in a given area. Predictability is especially crucial when it concerns a brewery's water supply.

The special contracts with PWW have allowed a great measure of certainty about rates and terms of service. Commission review and approval have ensured that rates reflect the costs of providing water to a customer whose unique situation makes general rate schedules inapplicable. The special contract process is open to public scrutiny, and protects the public interest by offering fair treatment of all customers.

When this proceeding began, Nashua could not state what rate AB would pay, what entity would set the rate in the future, what methodology it would use, whether an independent authority would review and approve the rate, and what procedure would be used to amend the rate. During the proceedings, the City proposed to have the Commission condition its approval on a number of commitments, some of which address these uncertainties. The Commission included those conditions in its order. From AB's perspective, a critical issue before the Court is whether the Commission will have continuing jurisdiction to ensure that Nashua complies with those conditions.

ARGUMENT

The City of Nashua seeks to take PWW's core water system by eminent domain pursuant to RSA 38, and to establish a municipal system serving its residents as well as certain customers outside the city limits, including Anheuser-Busch. The Commission conducted hearings to determine: (1) whether the proposed taking is in the public interest; and (2) if so, the value of PWW's assets to be taken. *See* RSA 38:9; RSA 38:11. AB participated in the hearings to protect its vital interest in its water supply.

I. Anheuser-Busch Defers to PUC Staff on Valuation Issues; AB Takes No Position on PEU and PAC, or on the Mitigation Fund.

Anheuser-Busch has a limited interest in the details of the valuation of PWW's system, and continues to defer to the considered analysis and judgments of PUC Staff concerning the validity and reliability of the parties' appraisal methodologies. AB takes no position on the Commission's decision to preclude Nashua's acquisition of PEU and PAC, or on the establishment or amount of a mitigation fund to protect the customers of those utilities.

II. Uncertainties About Future Rates and Service Bring into Question Whether Municipalization Will Serve the Public Interest.

The "public good" includes not only the needs of particular persons directly affected by an action, but also the needs of the public at large and the general welfare of the utility involved. *Boston & Maine Railroad v. State*, 102 N.H. 9 (1959). The record shows that PWW is a well-run utility. App. 75. PWW has extended service across municipal borders into areas experiencing supply problems – in at least once instance, where a municipally-owned system refused to do so. Day XI, pp. 33, 47, 102-103, 119-122. PWW has also served the public interest by acquiring a number of financially-troubled water systems.

Anheuser-Busch presumes that Nashua and Veolia could also provide good quality water at a fair price, be effective guardians of the watershed, and meet AB's need for clear communication and cooperative relations. However, municipalization inevitably creates uncertainties. Several areas remain of concern to AB.

A. Application of Cost Savings to Rates

The evidence suggests that the City could achieve some cost savings. App. 80. If those savings resulted in lower rates, they would be an important factor favoring municipalization. The Commission concludes that Nashua "intends to use its lower revenue requirement to lower customer rates." App. 80-81. If this Court confirms that the Commission's order is effectively conditioned upon the City passing savings along to ratepayers, AB is satisfied that the public interest will be served in this regard.

B. Future Decision-Making Authority

Several witnesses expressed the view that private companies have a profit incentive to expand their service territories across municipal boundaries, while competition between municipalities to attract new businesses to increase their tax bases can create a disincentive to cross-boundary cooperation. Day I, p. 198; Day XI, pp. 45-47, 105-106; Day XII, pp. 98-99. The Towns of Milford and Merrimack voiced serious reservations about the proposed taking. Day XI, pp. 14, 32, 63-64. The Town of Bedford did not support Nashua's petition unless the Regional Water District would control service in Bedford. Day XI, pp. 129-133. The fact that no municipalities unconditionally supported the petition may portend future frictions that would not serve the interests of the region as a whole.

Anheuser-Busch's facility is located in Merrimack. As a result, AB does not contribute directly to Nashua's property tax base, and after municipalization the company would have no

voice in decisions affecting its water supply. AB is concerned that ratemaking decisions could be influenced by political pressures unfavorable to large industrial customers located outside the city limits, unless Nashua's rates and service are subject to PUC jurisdiction. The Commission has played an essential role in ensuring the fair treatment of ratepayers in a transaction that is not subject to ordinary market forces.

AB was particularly troubled when the chief architect of Nashua's municipalization plan stated early on that City residents subsidize AB's special contract rate, and suggested that the City would eliminate special contracts. During the hearings, however, it became apparent that Mr. Sansoucy had based his conclusion about a subsidy on a mistaken belief that AB's special contract rate excludes any contribution toward PWW's administrative and operational costs. Day II, pp. 50-51. The evidence showed that the special contract rate in fact includes a contribution to PWW's overhead costs, consistent with an allocation derived from a cost of service study and approved by the Commission. It is now essentially undisputed that Nashua ratepayers do not subsidize AB's rate. App. 65; Day VII, p. 109; Day XII, pp. 74-75.

As discussed below, the Commission has stated its intent to ensure the fair treatment of customers located outside the City boundaries. App. 81-85. If this Court finds that the Commission retains jurisdiction to do so, that finding would significantly reduce AB's concern about future decision-making authority.

C. Special Contract vs. Tariff

RSA 38:17 authorizes municipalities to enter into water supply contracts. Anheuser-Busch asked the Commission to condition any approval of Nashua's petition on the City's assumption of the existing special contract, or on the execution of a substantially similar new contract. However, during hearings the City represented that it cannot enter into such a contract

without forfeiting the tax-exempt status of bonds used to fund the taking. Instead, AB's rate would be implemented through a tariff. Day I, pp. 158-159; Day II, p. 46; Day XI, pp. 19-20, 67.

Nashua's inability to serve AB through a special contract creates certain difficulties, principally with respect to enforcement. Unless Nashua is a regulated public utility, AB knows of no mechanism limiting the ability of a future board of aldermen – or a regional water district – to unilaterally amend or revoke a tariff. However, if the Commission continues to regulate Nashua's rates and service to AB, the distinction between service under a tariff versus service under a special contract is not necessarily critical. The public interest will be served provided the parties are free to negotiate rates that are fair and create proper incentives for conservation.

D. The Regional Water District

The Commission determined that it could not decide issues concerning the Merrimack Valley Regional Water District in this docket, as that entity's potential control of the water system in Nashua was not ripe for consideration. Anheuser-Busch understands the legal and practical difficulties of passing judgment on the future of a regional district that is largely hypothetical. Nevertheless, AB cannot realistically assess the ramifications of municipalization without recognizing that in the near future it would likely be dealing with an entirely different water provider, one that presented no witnesses in the proceeding. Day I, pp. 21, 95.

The legal rights and obligations of a regional water district have been a matter of debate, along with the Commission's regulatory authority over the transfer of assets to a regional district and over water rates and service by a regional district. Unlike Nashua, the Regional District has not offered to provide service on the same terms as PWW. It has not agreed to abide by any conditions the Commission has imposed on Nashua, or to submit its rates and service to Commission regulation.

The Commission states that under RSA 374 “any future transfer of Nashua’s franchise would remain subject to Commission jurisdiction.” App. 84. That comment falls somewhat short of an assurance that the Regional Water District will be subject to the same Commission oversight on rates and service as Nashua following any transfer of control of the water system to the Regional District.

III. The Viability of the Commission’s Order Depends Upon the Commission’s Authority to Exercise Ongoing Jurisdiction over Nashua’s Service and Rates to Customers Outside the City Limits.

During the hearings, Nashua recognized that a number of unresolved issues prevented the parties and the Commission from addressing material elements of the City’s proposal. To address those problems, the City asked the Commission to condition its approval on certain commitments not included in the original petition. Among those was a commitment to supply water to Anheuser-Busch in accordance with the terms of its current special contract, and a stipulation that service to AB would remain subject to Commission jurisdiction under RSA 362:4 and RSA 374. App. 73; Day I, pp. 118-119; Day II, pp. 45-46; Day X, pp. 206-207; Day XI, pp. 19-20, 61-62, 65-67, 81-82, 111-112; Day XII, pp. 155-156, 165-166.

AB appreciates Nashua’s efforts, and recognizes the difficulties of presenting in advance all the details of a plan for operating a water system. AB also recognizes, however, that changes in Nashua’s proposal created a “moving target,” and to some degree impaired other parties’ ability to conduct adequate discovery and to present their challenges to the City’s petition. Day XII, pp. 77, 108, 177-178. AB takes no position on whether the proposal and approval of conditions violated any party’s due process rights. App. 57. If the approved conditions are appropriate, and are enforceable, they allay many of AB’s concerns about the uncertain results of municipalization.

A. RSA 38:11

The owner or operator of a public water system is ordinarily deemed a regulated public utility. There is an exception for municipalities operating within their corporate limits. *See* RSA 38:14. A municipality's operations *outside* its limits, however, are subject to PUC jurisdiction except as provided in RSA 362. *See Blair v. Manchester Water Works*, 103 N.H. 505, 507 (1961). The precise parameters of that jurisdiction were a matter of contention in these proceedings. The fundamental dilemma is that the Commission's express authority to set conditions on approval of municipal water service may be at odds with its apparent loss of jurisdiction over the municipality as soon as it issues that approval. *See* RSA 362:4. If the statutes deprive the Commission of subject matter jurisdiction to regulate municipal water systems, it is doubtful that parties may confer that jurisdiction by agreement. Unless the Commission can lawfully exercise that jurisdiction, the uncertainties of municipalization are extremely problematic.

In approving municipalization, the Commission has authority to set conditions to ensure that the public good is satisfied. RSA 38:11. That statute does not describe the scope of permissible conditions, or any means of enforcing them. The Commission states that:

While this authority is not limitless, it surely allows us to bind an acquiring municipality, especially to commitments it has made that have the effect of causing it to function in some respects as if it were a regulated public utility, as long as a reasonable nexus exists between those commitments and the public interest considerations at issue in the proceeding. For this reason, we proceed with our analysis of the record with the assumption that it is lawful to set conditions which fall squarely within the realm of utility regulation, and that we will maintain continuing authority to enforce any conditions.

App. 50 (footnote omitted). Although it refers to an "assumption" about its continuing enforcement authority, the Commission subsequently conducts an analysis supporting its

conclusion that the legislature did not intend RSA 362:4 to limit its authority to set and enforce conditions. App. 84-85.

B. RSA 362 and RSA 374

A municipality providing service outside its borders is not a public utility for purposes of “accounting, reporting, or auditing functions.” RSA 362:4, II. It is not a public utility if it offers *new* customers outside its municipal boundaries the same service it offers municipal customers, at a rate no more than fifteen percent higher than the rate it charges municipal customers. RSA 362:4, III-a (a)(1). The term “new customers” apparently refers to customers served by an expansion of a municipal system occurring after May 13, 2002, and therefore would not include customers such as Anheuser-Busch. *See* RSA 362:4, III-a(c).

The Commission finds that pursuant to RSA 362:4, III-a(b), Nashua will generally continue to be subject to the Commission’s jurisdiction, although it will be exempt from accounting, reporting, and auditing functions pursuant to RSA 362:4, II. App. 79. The Commission also states that it will continue to exercise the authority to review and approve rates for service outside Nashua’s municipal boundaries App. 82. “RSA 362:4 clearly provides that all municipal corporations serving outside their corporate boundaries are not exempt from the franchise requirements of RSA 374.” App. 83-84. “[W]e cannot conclude that the Legislature intended RSA 362:4 to limit [...] the Commission’s ability to ensure the public interest is satisfied under RSA 38:11.” App. 85.

The Commission is likely correct in its view that the authority to impose conditions under RSA 38:11 would be meaningless unless the legislature also intended to allow the Commission to enforce its conditions. It is also apparent that the legislature intended RSA 362:4, III and III-a to ensure fair treatment of all customers of a municipal water company. In interpreting the

interplay of these statutes, the Court should read the statutory scheme as a whole and strive to implement the legislature's intent.

IV. The Commission's Order Must Be Construed to Provide Continuing Regulatory Authority Over Both Service and Rates.

The Commission's conditions include the following:

Nashua shall provide service to all PWW's wholesale users in accordance with the rates, terms, and conditions of all existing wholesale contracts either by adopting those contracts outright or, if required for bonding purposes, by filing with the Commission a wholesale tariff that incorporates the rates and provisions of the existing wholesale contracts.

App. 122. In the section of the order enumerating the conditions it is imposing, the Commission does not expressly state that it will retain jurisdiction to approve rate changes and any proposed amendments to the contracts/tariffs. However, in its statutory analysis the Commission makes clear that:

[...] Nashua, to the extent it provides service outside its municipal boundaries, will be regulated by the Commission, [...] and [...] may not raise rates unless there is a cost basis for doing so and the Commission approves such an increase.

App. 82.

[W]e have broad authority to set conditions pursuant to RSA 38:11, which allows us to subject Nashua to the same oversight with respect to wholesale water supply contracts as that to which PWW is currently subject.

App. 85. Accordingly, if it affirms the PUC's order, the Court should confirm that the Commission's ongoing jurisdiction includes the authority to review and approve rate increases in accordance with its standard criteria, requiring a showing of valid cost bases for increases and excluding costs that are not prudently incurred.

CONCLUSION

This Court is in a position to clarify the Commission's authority to set conditions on its approval of Nashua's petition, and the Commission's ongoing jurisdiction to enforce those conditions. If the Commission retains full jurisdiction over rates and service outside the City's boundaries, and over the rates and services of any successors to the City's operations, Anheuser-Busch has no objection to municipalization. However, if the Court determines that the Commission cannot both set and enforce the conditions discussed above, Anheuser-Busch believes municipalization will not be in the public interest.

Respectfully submitted,


ANHEUSER-BUSCH, INCORPORATED

By Its Attorneys

RANSMEIER & SPELLMAN
PROFESSIONAL CORPORATION

Dated: September 29, 2009

By:




John T. Alexander (#6795)
Daniel J. Mullen (#1830)
One Capitol Street
P.O. Box 600
Concord, NH 03302-0600
(603) 228-0477

ORAL ARGUMENT

Anheuser-Busch does not request oral argument.

CERTIFICATE OF SERVICE

I hereby certify that two copies of this brief have been sent this day by first class mail to all counsel and *pro se* parties listed on the Court's distribution list.



John T. Alexander

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