STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Joint Petition of Fortis, Inc. et al.
and CH Energy Group, Inc. et al.
for Approval of the Acquisition of **Case 12-M-0192**
CH Energy Group, Inc. by
Fortis, Inc. and Related Transactions

BRIEF ON EXCEPTIONS
OF
PUBLIC UTILITY LAW PROJECT OF NEW YORK, INC. (PULP)

May 17, 2013

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PRELIMINARY STATEMENT

This proceeding is examining whether the Commission should authorize or reject the Petition of CH Energy Group, Inc. ("CHEG"), parent of Central Hudson, and Fortis, Inc. ("Fortis"), a foreign holding company, for acquisition of CHEG by Fortis, including their proposal for continuation for one year of the current multi-year rate plan that would otherwise conclude on June 30, 2013. The Public Utility Law Project of New York, Inc. ("PULP") is a not-for-profit organization dedicated to advancing the interests of residential customers in utility and energy related matters with an emphasis on addressing the special needs and interests of low-income consumers, including residential customers in the Central Hudson Gas & Electric Corporation ("Central Hudson") service territory. PULP is an active party in this proceeding, and filed initial testimony.[1] Due to resource limitations and a funding hiatus, PULP was not able to participate fully in all phases of this case. (See PULP Initial Comments on Joint Proposal, filed February 8, 2013, at 1-2).

The litigation schedule was changed, and hearings cancelled, after several parties reached agreement on a Joint Proposal for resolution of the proceeding. PULP filed initial and reply comments opposing the Joint Proposal. In response to community opposition, the Commission held additional public statement hearings

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[1] PULP's witness pointed out that interruption of service to Central Hudson customers for bill collection purposes increased dramatically, from 4688 in 2005 to 12,704 in 2011, and were higher year to date in 2012 when her testimony was filed. She recommended, *inter alia*, enhancement of low-income rate reductions including a per-therm rate reduction for low-income gas heating customers, higher participation and expanded eligibility for the reduced rates, formalization of a low-income rate classification; reform of collection practices, including metrics to reduce the reliance upon service interruption as a bill collection measure, and improved call center performance metrics. See Testimony of Barbara R. Alexander filed October 12, 2012.

and extended the period for receipt of public comments. Public comments were overwhelmingly opposed to the acquisition of Central Hudson.

A Recommended Decision was issued on May 3, 2013 by Administrative Law Judges Rafael A. Epstein and David L. Prestemon. In accordance with the Notice for Filing Exceptions, issued by the Secretary of the Public Service Commission ("Commission") on May 3, 2013, PULP submits this Brief on Exceptions.

SUMMARY OF POSITION

PULP generally agrees with the Judges' Recommendation that the proposed merger and acquisition be rejected by the Commission, and is in full agreement with their "opinion that the proposed transaction's flaws may be inherently unsusceptible to effective remediation by means of supplemental [Positive Benefit Adjustments]." (RD at 67). Accordingly, their identification of detriments to the proposed transaction, and their conclusion that these detriments are inherently irreparable, will not be reiterated. The following exceptions are taken by PULP only with regard to certain findings contained in the Recommended Decision and certain omissions because, although they did not ultimately affect the correct conclusion of the Judges, they provide additional grounds upon which the Commission should reject the Joint Proposal for merger and the rate plan extension.

PULP takes the following exceptions:

- The Joint Proposal failed to win the support of any independent representative of residential ratepayers;

- The continuation of the existing rate plan is unreasonable because it fosters inordinate storm damage risk and fosters inadequate disaster risk prevention, perpetuates aggressive service termination practices, provides insufficient protections to low-income customers, and negates a thorough examination of rates that could correct potential overearnings;
- The $35 million to be recorded as a regulatory liability to offset and write down deferred storm restoration expenses in future proceedings is a poor substitute for immediate rate reductions;
- The "golden share" offered to be held by a trustee approved by the Commission to "ring fence" Central Hudson from voluntary bankruptcy of its parent is inadequate because it is against Fortis' own investor rules, may be voidable or its effectiveness diluted due to international cross-border insolvency and NAFTA rules;
- There are insufficiently mitigated risks from possible follow-on mergers,
- There are risks arising from the NAFTA Chapter 11 investor protections, and legal divergence between U.S. regulatory taking standards and NAFTA.

EXCEPTIONS

POINT I

THE RECOMMENDED DECISION ERRED IN FINDING THAT THE JOINT PROPOSAL HAS THE SUPPORT OF ANY INDEPENDENT REPRESENTATIVE OF RESIDENTIAL RATEPAYERS

The Joint Proposal is a non unanimous settlement agreement among some of the parties to the case who agreed to the merger on conditions contained in their

proposal. The Commission's Settlement Guidelines provide deference to settling parties' accommodations when agreement is reached among numerous, normally adversarial parties to avoid litigation of the merits of issues and the agreed-upon resoluton is consistent with law and Commission policy. The Recommended Decision erred in its finding that the support of the Department of State's Utility Intervention Unit ("UIU"), along with that of Multiple Intervenors and Ulster, Dutchess and Orange County Executives[2], is "a valid indicator of the fact that the Joint Proposal represents a compromise of interests that often are, and were initially in this case, adverse." (RD at 50).

PULP takes exception to the finding that the settlement is adequately supported by normally adverse interests, (RD at 50), and maintains its position that there is insufficient basis for the Commission to give any deference to the settlement process results embodied in the Joint Proposal because there is no support from any party possessing the indicia of structural independence expected of residential utility consumer advocates, while there is evidence of overwhelming opposition from residential customers of Central Hudson. The flaws in the structure and resources for residential consumer advocacy confront the legitimacy of the administrative litigation, stakeholder processes and alternative dispute resolution efforts in this case.

The Recommended Decision, however, found that the Department of State's utility Intervention Unit ("UIU") retains the consumer protection mandate of its

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[2] The Ulster County legislature, by resolution, and a majority of the members of the Dutchess County legislature, by letter, oppose approval of the proposal, diminishing the force of the support from the two county executives.

predecessor agency, the Consumer Protection Board." (RD at 49), and thus gives credence to UIU's support for the Joint Proposal. PULP takes exception to that finding.

The Recommended Decision erred, because did not inherit the limited powers that its predecessor, the Consumer Protection Board once had, before that office was abolished and some of its functions transferred to the Department of State. For example, under current law, the UIU has no express power to seek judicial review of utility actions or rulings of utility regulatory agencies. Its inability to take legal positions separate and distinct from the Secretary of State and ultimately the Governor is inconsistent with being an independent voice at the table for residential customers.

Originally, when the Consumer Protection Board was first formed, it, as is the case with the current UIU, had no express statutory power to seek judicial review of PSC orders. Rosemary Pooler, then CPB director, attempted to challenge a PSC rate case order on behalf of consumers but the courts squarely held that without express statutory power she and the CPB lacked power to challenge the PSC order.[3] The definitive decision of the state's highest court was that express power of CPB to seek judicial review was necessary but lacking. A very narrow response to cure the deficiency identified in the *Pooler* case was adopted by the legislature in L. 1978, c. 120. That law gave power to the CPB Director on his or her own motion to seek judicial review of PSC decisions "involving the establishment of rates."[4]

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[3] *Pooler v PSC*, 89 Misc.2d 700 (1977), *affirmed*, 58 A.D.2d 940 (1977), *affirmed* 43 N.Y.2d 759 (1977).
[4] The curative amendment did not give CPB power to participate in judicial review of FERC or FCC cases, or in merger cases, or in cases like the recent federal antitrust cases involving NYISO market

When the CPB was recently abolished, the legacy utility intervention function was transferred to the successor UIU within the Department of State. But the actual language of the new Executive Law §94-a(4) which accomplished the transfer of CPB functions to the UIU does not authorize the director of the UIU to participate in any court proceedings. Indeed, the law does not mention and creates no office of the UIU director, and it specifically authorizes the UIU to represent consumers only in administrative proceedings.[5] UIU is only given specific authority to represent customers in administrative proceedings in energy cases, and not in cases involving other utilities, including telecom, water, or cable. Also, there is no express authority for the UIU to represent residential consumers in other matters affecting utility customers, such as antitrust cases[6] or declaratory judgment or injunction actions brought by utilities against regulators which could adversely affect New York residential customers.[7]

For the system of interest group representation and alternative dispute resolution to work in the manner intended it is pivotal for residential ratepayers to have their rights as major stakeholders vigorously protected. This

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manipulation. Also, it did not grant specific power to seek judicial review of rulemaking orders, petitions, or other orders that do not establish new rates.

[5] In contrast to the limited power to "represent the interests of *consumers*" in energy cases only, the existing law gives the UIU slightly broader power to intervene in complaint type proceedings "*on behalf of the secretary*, to the extent authorized by sections twenty-four-a, seventy-one, eighty-four or ninety-six of the public service law or any other applicable provision of law, where he or she [the secretary of DOS] deems such initiation, intervention or participation to be necessary or appropriate...." Executive Law §94-a(4)(b)(i). (*Emphasis supplied*). The cited sections are complaint type proceedings, and not rate proceedings, generic industry wide proceedings, or rulemaking proceedings which often affect residential consumer interests.

[6] *See U.S. v. Morgan Stanley*, 881 F. Supp. 2d 563 (S.D.N.Y. 2012) and *United States v. Keyspan Corp.*, 763 F.Supp.2d 633, 636 (S.D.N.Y.2011) (settling cases alleging manipulation of NYISO capacity markets costing New York consumers hundreds of millions of dollars for 20-25% of gains with no admission of wrongdoing).

[7] *See Indeck Corinth v. Paterson*, Index No. 5280/2009, (N.Y. Sup. Ct., Albany Co., filed Jan. 29, 2009) (challenging RGGI under state and federal law).

requires effective consumer representation through residential ratepayer advocates emboldened with full inquisitorial and discovery powers, sufficient financial support to act as an effective counterweight to the resources of the utilities, and structural independence of the advocates, to protect against the appearance that direct or indirect political decisions or considerations may dictate the positions taken in major cases such as this. Credibility of a residential utility consumer advocate not only requires the ability to know the voluminous record of a case, conduct discovery, put on direct and rebuttal written testimony of experts, participate in expert cross examination when there are hearings, participate in confidential settlement negotiations, make and respond to motions, and file briefs with ALJs and the regulatory commission. It also requires the ability, like other intervenors, to seek judicial review of utility and regulatory actions in appropriate situations. While most work of consumer advocates is administrative, there are ample illustrations of cases where state utility consumer advocates have defended the rights of residential consumers and won victories.[8] For example the North Carolina Supreme Court recently ruled in favor of the independent utility advocate representing the interests of North Carolina's residential ratepayers in a case involving the North Carolina Utilities Commission approval of a 7.2 percent increase in electricity rates for Duke Energy Carolinas, which represented a 10.5 percent return on equity.[9]

The absence of independent, adequately funded and empowered

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[8] *See, e.g., Duquesne Light Co. v. Barasch*, 488 U. S. 299 (1989); *Maryland People's Counsel v. FERC*, 761 F.2d 768 (D.C. Cir. 1985).

[9] *See State ex rel. Utils. Comm'n v. Attorney Gen.*, Op. No. 268A12 (N.C. Ct. App. filed April 12, 2013), available at http://appellate.nccourts.org/opinions/?c=1&pdf=MjAxMy8yNjhBMTItMS5wZGY=

representation of residential customers places New York out of step with the relevant standard setting organization the National Association of State Utility Advocates ("NASUCA"). The Constitution of NASUCA requires its members to be independent with respect to "policy determination, hiring and firing of personnel, and fiscal control," to be separate from the regulatory commission, and capable of seeking judicial review of regulatory decisions.[10] UIU is lacking in these attributes of independence.

The Recommended Decision takes note of PULP's argument but insists, "PULP neglects to point out, however, that UIU is, in fact, a member of NASUCA." (RD at 49). Far from a glaring oversight by PULP, the ALJs failed to recognize that UIU is actually not listed as a full Member of NASUCA but is instead the only state agency listed as an "Associate Member,[11] a lesser category of membership for agencies not meeting the requirements of full membership, with less rights in governance of NASUCA.[12] UIU is the only state agency in NASUCA that is not a full member. Moreover, even if UIU were to be considered a member of NASUCA, or if NASUCA waived its independence requirements, that alone does not confer upon it the actual independence necessary for a bona fide independent representative of residential customer interests in the Commission's stakeholder processes. UIU's backing of this merger should be discounted because no independent residential consumer advocate supports this merger.

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[10] NASUCA Constitution, Art. III, Sec. 1, available at http://www.nasuca.org/archive/NASUCA%20Constitution.pdf.

[11] *See* NASUCA Membership http://www.nasuca.org/archive/about/membdir.php for a current directory of NASUCA members.

[12] *See* History of NASUCA, available at http://www.nasuca.org/archive/about/index.php

POINT II

THE RECOMMENDED DECISION ERRONEOUSLY FOUND BENEFITS TO THE TRANSACTION AND EXTENSION OF THE EXISTING RATE PLAN

The Recommended Decision found tangible benefits in the Joint Petitioners' proposed $35 million regulatory liability for storm recovery, $5 million in Community Benefit Fund, $500,000 of which will assist low-income customers, and the $9.25 million of synergy benefits spread over five years, for a total customer benefit of $49.25 million. (RD at 63).

The $35 Million Regulatory Liability. The bulk of these benefits are accounting offsets in future rate cases, and thus should be discounted. These include the claimed $9.25 million in synergy savings and "Guaranteed Rate Reductions" spread at $1.85 million a year for five years (Joint Petition at 49), $35 million in deferred storm restoration cost write-offs and future rate mitigation, most of which is eaten by claims arising from prior storms, leaving only a credit towards future storms of $13 million (Joint Petition at 49-52),[13] and $5 million in Community Benefits that require future consensus and Commission approval (Joint Petition at, 42-44). A dollar today is always better than a dollar tomorrow and promises of future offsets of some claims within a larger rate case context where unknown future utility claims are also in play are a poor substitute for immediate rate reductions, which have been achieved in mergers where significant benefits exist.

The write-off of storm cost deferrals is not as concrete a benefit as the

[13] After the Joint Proposal was filed, Central Hudson claimed an additional $9.7 million deferral of Superstorm Sandy costs, which is the subject of another proceeding, and which was opposed by PULP. See Case 13-E-0048, *Petition of Central Hudson Gas & Electric Corporation for Approval to Recover Deferred Incremental Costs.*

Petitioners urge and as the Recommended Decision found. Once rates are set, recovery from customers when costs turn out to be higher than expected is normally not allowed under the filed rate doctrine and a general rule against retroactive ratemaking. Thus, recoupment of unanticipated losses is ordinarily barred, and deferral petitions ordinarily are subject to strict regulatory scrutiny. The following conditions for deferral of unanticipated costs usually apply:

1. The cost must be material.[14]
2. The cost must be unusual, and not reasonably forecast in a rate proceeding.
3. The deferral request must be incremental to the amount currently allowed in rates.
4. The utility cannot be over-earning its allowed return on equity, or overearn if the deferral is allowed.
5. The company must show it attempted to mitigate the expense.

Under the Joint Proposal, Central Hudson receives a great benefit by not having to satisfy all these standards for recovery of deferred costs, and instead is trading away its untested and unadjudicated deferral claims as if they were sure to be recovered in the absence of the merger. It is possible, however, that Central Hudson could be in an overearning situation if it were to recover the deferral claims.[15] Or, some of the deferred storm costs are already anticipated in existing rates, and not incremental, or charges may be inflated or unsupported. Or, inadequate tree trimming and maintenance prior to the storms exacerbated the damage. Sacrificing the deferral claims as a merger chit may not be worth the claimed amount of

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[14] "The Commission's current policy on materiality is that an item must exceed 5% of the company's net income to qualify for deferred accounting treatment." Case 01-G-1821, *Petition of Central Hudson Gas & Electric Corporation for Approval for Environmental Site Investigation and Remediation Costs, filed in C 9218*, Issued Oct. 25, 2002.

[15] Notably, Central Hudson has not sought to change its rates even though it could have.

benefits because absent the merger, the deferred claims may be more closely scrutinized and disallowed.

Continuation of the rate plan poses added storm damage risks to consumers. The "revenue decoupling" features of the current plan diminish the incentive of Central Hudson to restore power quickly in storm scenarios, because Central Hudson is guaranteed the same revenue whether meters are spinning or not. Toothless "performance regulation" metrics in the current plan do not penalize weak storm damage prevention or sluggish recovery from major storms, and incentivizes skimping on maintenance. Another storm could quickly wipe out the balance of the balance of the $35 million putative ratepayer benefits.

In its Initial Brief, PULP advocated that if this merger is approved it should be conditioned upon increasing the material benefits for customers, especially low-income ratepayers (PULP Initial Brief at 14-16). Those protections, advanced by PULP's expert witness Barbara R. Alexander[16] were intended offset some of the risks that customers could be exposed if the proposed transaction is approved.

Terminations. Approximately 12,000 Central Hudson residential customers experience the hardship of service interruption for bill collection purposes each year, and approximately 23,000 are more than 60 days behind in paying their bills, owing more than $12 million. The current rate plan allows for aggressive termination practices imposed upon economically distressed customers.

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[16] Case 12-M-0192, Testimony of Barbara R. Alexander, (submitted October 12, 2012), publicly available at http://documents.dps.ny.gov/public/Common/ViewDoc.aspx?DocRefId={9E9E2E56-180F-488E-9154-A933D049005A}

The Recommended Decision appears to find these tactics to be a virtuous exercise against economic "free riding," claiming "[r]estricting terminations does not promote equity; it simply increases the burden of uncollectible bills for all customers." (RD at 49). The fact that so many Central Hudson customers find themselves in arrears lends credence to the assertion by PULP that there exist inadequate protections for low-income consumers and failure in setting optimal, and thus progressive, tariff structures that maximize social welfare and human development within the service area.[17] In regulated markets such as energy where price schedules carry with them strong social consequences and potential for economic distortions, it is crucial that pricing appropriately balances equity and efficiency.

Limiting aggressive terminations aims at rectifying these imbalances and restores equity to a regressively priced system. The aggressive terminations take a heavy toll on families and communities when customers are without service and in desperate and chaotic situations. The importance of continuous electric utility service was underscored by Superstorm Sandy. Outages are forceful reminders of the essential role of reliable electric service to consumers in today's world. Continuous electric service is essential for household lighting, refrigeration, cooking, and in many circumstances, for heating, cooling, sanitation, water supply, elevator service, telephone and internet service. When electric service is interrupted, household life quickly becomes chaotic, and there is increased risk of illness or

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[17] *See generally* Feldstein, M. *Equity and Efficiency in Public Sector Pricing: The Optimal Two-Part Tariff.* Quarterly Journal of Economics. 1972;86 *(May).*

possible death of persons vulnerable to heat or cold. Society as a whole faces significant costs from unsafe or unhealthy situations in the absence of utility service. Public health and safety are impaired requiring emergency aid and medical care when households whose utilities are shut off resort to less safe energy sources. Central Hudson's rate structure should generally be made more equitable, fortified with added low-income protections, and collection efforts should reflect deference towards economically vulnerable populations.

POINT III

THE RECOMMENDED DECISION ERRONEOUSLY FOUND FINANCIAL PROTECTIONS WERE ADEQUATE BECAUSE THE "GOLDEN SHARE IS AGAINST FORTIS' OWN INVESTOR RULES, AND MAY BE VOIDABLE DUE TO INTERNATIONAL CROSS-BORDER INSOLVENCY AND NAFTA RULES

Experience in the Enron and Constellation cases teaches than seemingly solid holding company empires can collapse or be impaired rapidly. Major legal and substantive deficiencies in one of the main pillars of Joint Petitioners' bulwark against credit downgrades and insolvency buffers adds to a growing list of detrimental risks which have not yet been adequately mitigated and indemnified against. In the event this merger is approved as currently structured the Joint Proposal offers as a protection against Central Hudson from entering into voluntary bankruptcy at the demand of its parent company Fortis the creation of a special class of Central Hudson preferred stock to be held by an undesignated trustee approved by the Commission, otherwise known as "golden shares." These golden shares are offered to appease concerns over the shaky credit rating of Fortis and are proposed as a mitigation tool to assuage the Commission of the difficulty of policing

and monitoring the riskiness in far-flung public utility holding company structures and dealings.[18] However secure a golden share may sound, relying on an alleged corporate governance gold standard imbues a false sense of security.

A golden share held by a Commission anointed trustee would not guarantee that Central Hudson need to restrain from filing a petition for bankruptcy, as all board members would still remain beholden to the corporate governance fiduciary obligations of loyalty to shareholders, which would encompass the parent corporate entity as a whole. Furthermore, there is no explicit requirement that a golden shareholder must vote against the utility's filing for a voluntary petition for bankruptcy. The Bankruptcy Court for the Southern District of New York, which covers Dutchess County where Central Hudson is located, clarified in a major bankruptcy proceeding the "belie[f] that an 'independent' manager can serve on a board solely for the purpose of voting 'no' to a bankruptcy filing because of the desires of a secured creditor[is] mistaken."[19] Similarly, it cannot be assumed that an unnamed trustee will do the right thing for customers.

Fortis's own documents outlining Fortis Investments' expectations of public

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[18] "The growth of the holding company systems has frequently been primarily dictated by promoters' dreams of far-flung power and bankers' schemes for security profits, and has often been attained with the great waste and disregard of public benefit which might be expected from such motives. Whole strings of companies with no particular relation to, and often essentially unconnected with, units in an existing system have been absorbed from time to time. The prices paid for additional units not only have been based upon inflated values but frequently have been run up out of reason by the rivalry of contending systems. Because this growth has been actuated primarily by a desire for size and the power inherent in size, the controlling groups have in many instances done no more than pay lip service to the principle of building up a system as an integrated and economic whole, which might bring actual benefits to its component parts from related operations and unified management. Instead, they have too frequently given us massive, over-capitalized organizations of ever- increasing complexity and steadily diminishing coordination and efficiency ." Report of the National Power Policy Committee on Public-Utility Holding Companies, H.Doc. 137, 74th Cong., 1st Sess., p. 5, quoted in *North American Co. v. Securities and Exchange Com'n*, 327 U.S. 686, 703 (1946).

[19] *See* Strauss, Scott and Hopkins, Peter, *The Constellation Experience: Ring-fencing after the subprime meltdown*, quoting *In re Gen. Growth Props., Inc.*, No. 09-11977, slip op. at 33 (Bankr. S.D.N.Y. Aug. 11, 2009), available at http://www.spiegelmcd.com/files/20100825_ConstellationExperience.pdf

companies in which they invest undeniably states that as a policy it is adamantly against golden shares and will vote against them whenever it can. Section 4.17 of its own governance and voting principles titled Voting Rights Distortions makes clear:

Fortis Investments will vote AGAINST:

- Multiple Voting Shares
- Non-Voting Depository Receipts
- Ownership ceiling
- Voting right ceiling
- Priority shares
- Golden share

Fortis Investments: Governance and Voting Principles, at 14, August 2008. [20]

Whispering sweet golden share reassurances into the ears of the regulators while espousing distain for such voting rights to investors should raise serious alarm bells. Fortis' stated intentions appear to oppose the interests of any golden shareholder, thus converting this risk mitigation instrument into fool's gold. In light of such a stark contradiction one must question how many more golden promises contained in the Joint Petition could in time pan out to be tin.

The European Court of Justice has in numerous cases struck down golden share arrangements as derogation from traditional corporate law and an infringement upon movement of capital and the freedom of establishment.[21] In

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[20] Available at http://www.obam.nu/documents/fortis_obam_proxy_voting_on_internet.pdf

[21] *See* Case C- 58/99, *Commission v. Italy*, (2000), ECR I-3811; Case C-367/98, *Commission v. Portugal*, (2002), ECR I-4731; Case C-483/99, *Commission v. France*, (2002), ECR I-4781; Case C-503/99, *Commission v. Belgium*, (2002), ECR I-4809; Case C-463/00,*Commission v. Spain*, (2003), ECR I-4581; Case C-98/01, *Commission v. United Kingdom*, (2003), ECR I-4641; Joined Cases C-282/04 and C-283/04,*Commission v. The Netherlands*, (2006), ECR I-9141; C-174/04, *Commission v. Italy*, (2005), ECR I-4933; Case C-112/05, *Commission v. Germany*, (2007), ECR I-8995; Joined Cases C-463/04 and C-464/04, *Commission v. Italy*, (2007), ECR I-10419; Case C-274/06, *Commission v. Spain*, (2008), ECR I-0026; Case C-326/07, *Commission v. Italy*, (2009), ECR I-2291; Case C-171/08; *see generally* Camara, P., *The End of the "Golden" Age of Privatisations? - The Recent ECJ Decisions on Golden Shares* 3 EBOR (2002).

addition to a U.S. Bankruptcy court potentially ruling in line with European counterparts in striking down golden shares, Fortis might satisfy its pledge to investors to oppose golden shares by also challenging it in a NAFTA tribunal. Article 102 of the NAFTA states that "the objectives of this Agreement . . . are to" . . . (c) increase substantially investment opportunities in the territories of the Parties. . ."[22] As the thrust of NAFTA Chapter 11 investor rules (discussed in greater detail below) is to protect the rights of investor from one signatory country in other as enumerated by the NAFTA treaty, it is conceivable Fortis could challenge under NAFTA the state action inherent in a Commission approved golden shareholder as an infringement of its investor rights to full enjoyment and use of its financial investment in Central Hudson.

Even if it is believed that the golden shareholder sufficiently restrains Central Hudson from entering into voluntary bankruptcy, what restrains the U.S. Fortis holding company, which owns Central Hudson, from seeking relief in bankruptcy, or the parent Fortis Inc. from seeking bankruptcy relief in Canada? International cross-border insolvency rules might complicate, and thus dilute, any perceived protection afforded Central Hudson ratepayers. Chapter 15 of the U.S. bankruptcy code case is based on the Model Law on Cross Border Insolvency, which had been prepared by the United Nations Commission on International Trade Law (UNCITRAL).[23] Chapter 15 allows parties in U.S. bankruptcy courts to seek recognition of a foreign proceeding by a foreign representative. 11 U.S.C. § 1504.

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[22] North American Free Trade Agreement, Dec. 17, 1992, U.S.-Can.-Mex., 107 Stat. 2057 (1994), 32 I.L.M. 605 (1993) [hereinafter NAFTA]. Article 102,, available at http://www.nafta-sec-alena.org/en/view.aspx?conID=590&mtpiID=122#101

[23] *See generally U.S. v. J.A. Jones Constr. Group*, LLC, 333 B.R. 637, 638 (E.D.N.Y. 2005)

There is a risk that Chapter 15 rules could force U.S. courts to recognize bankruptcy proceedings initiated in Canada by the parent Fortis seizing or impairing U.S. Fortis and Central Hudson assets to satisfy creditors.

POINT IV

THE RECOMMENDED DECISION ERRONEOUSLY DISCOUNTS RISK DUE TO POTENTIAL NAFTA LIABILITY

The Recommended Decision discusses the legal authorities cited by PULP regarding the legal risk stemming from NAFTA Chapter 11 investor projections but concludes that since there are no reported cases specifically involving a public utility regulatory agency acting within the scope of its statutory authority that faced a claim of nationalization or expropriation under NAFTA Fortis's status as an investor from a NAFTA member state the possibility "does not add any significant risk to the transaction." (RD at 46). The rationale is in part based on the ALJs interpretation of NAFTA tribunal case law that "a state regulatory agency acting lawfully within its statutory authority is not liable to a claim of damages under NAFTA unless an entity covered by the treaty can demonstrate that it made its investment in the state pursuant to express commitments made by the agency which were subsequently broken NAFTA." (RD at 46). PULP takes exception to the view that NAFTA rules are innocuous to the regulatory authority of the Commission and pose no risk to consumers if this transaction were to be approved.

Deviating from the ALJs belief that that indirect expropriation could only be found if express commitments are broken, the arbitration panel in Metalclad Corporation v. The United Mexican States illuminates that the test examines only the

impact of a challenged measure on an investment, rejecting traditional regulatory police powers in favor of private rights over state interference:

> "Thus, expropriation under NAFTA includes not only open, deliberate and acknowledged takings of property ... but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be expected economic benefit of property even if not necessarily to the obvious benefit of the host state."[24]

NAFTA confers radical neo-liberal rights to foreign investors to attack routine exercises of state regulatory police power to protect public health, safety, welfare, and the environment.[25] NAFTA is not a harmless shield for investors as the ALJs assume, but is a penetrating sword that could inflict damage to the regulatory protections currently afforded Central Hudson consumers. As stated by Department of Public Service in its testimony filed before the staff agreed to the merger "Fortis is entering a very different regulatory environment than it has been operating under to date." (Prepared Corrected Staff Policy Panel Testimony at 23).[26] It is highly foreseeable that a Commission rate case determination may offer a rate on equity that would disappoint Fortis investors, or that the Commission might deny a request to invest in and build a facility such as a power plant on property owned by Central Hudson, or deny a request to invest in costly infrastructure to bulk up rate base and the return of and on investment. Central Hudson as a domestic entity today would

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[24] *Metalclad Corporation v. The United Mexican States*, ICSID Case No. ARB(AF)/97/1, para. 103, award available at http://www.italaw.com/sites/default/files/case-documents/ita0510.pdf

[25] *See generally* Poirier, Marc R. *NAFTA Chapter 11 Expropriation Debate through the Eyes of a Property Theorist,* 33 Envtl. L. 851 (2003).

[26] Case 12-M-0192, Prepared Corrected Testimony of Staff Policy Panel, (submitted October 2012 though corrected on November 5, 2012), available at http://documents.dps.ny.gov/public/Common/ViewDoc.aspx?DocRefId=%7b7870853C-A830-415A-A383-B4FC8FED5BC6%7d

have little recourse in this scenario outside of the U.S. legal system, but Fortis as a Canadian investor could invoke NAFTA Chapter 11 arbitration and challenge the Commission's decisions.

Even assuming arguendo that NAFTA investor protections do not create a strict liability against regulatory diminution of value of foreign investment, but is malleable to the expectations of the two parties as the ALJs argue, the unanswered question still remains what are the express commitments that the Commission would be making to Fortis if it were to approve this transaction? As Central Hudson is a regulated public utility though its capital structure attracts private capital there exists a natural tension between the competing public-private interests. To strike a reasonable balance New York Public Service Law requires that rates be "just and reasonable," and set by the Commission. As simple as that may sound, there is ample room for interpretation as to what in fact constitutes just and reasonable, and if Fortis were to be disappointed with a final determination by the Commission even under the expropriation interpretation put forth by the ALJ the Petitioners have not met the burden to disprove that Fortis would be fully precluded from seeking extrajudicial review by a NAFTA arbitral panel.

Furthermore, the possibility of a follow-on upstream merger scenario that PULP brought up in the initial comments (PULP Initial Brief at 4-5) raises jurisdictional questions not given due consideration by the Recommended Decision. It still remains unclear whether Fortis could transfer the U.S. holding company, which would own Central Hudson, to yet another entity, perhaps another foreign holding company, without PSC approval, and without providing any further public

benefits or mitigating risks. See Lisa Gayle Bradley, *On The Acquisition Of Upstream Interests In New York Energy Operating Companies – An Uncharted Area?,* 31 Energy Law Journal 509 (2010).[27] This issue is left ambiguous by the Joint Proposal, which only addresses shared synergy savings from follow-on mergers before the next rate case. Future PSC action attempting to prevent Fortis from exercising a risky upstream merger could be challenged under state law on jurisdictional grounds, or under NAFTA, thus adding further volatile legal risk to this transaction.

Fortis has not hesitated from invoking the protection of NAFTA when it suits its needs.[28] Nonetheless, Petitioners dismiss substantiated legal risks emanating from NAFTA as a "red herring." (Petitioners Additional Comments at 25) and distract from a nuanced legal discussion by mocking the genuine disquiet of public commenters as inarticulate buffoons. (Petitioners Additional Comments at 25-26). Despite Petitioners' insistence that NAFTA poses no real threat to the regulatory regime of the Public Service Commission, they do not refute PULPs claim that NAFTA confers rights that are not afforded purely domestic parties. To elucidate, NAFTA jurisprudence on regulatory taking is not bound by U.S. Constitutional laws,

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[27] "This Article undertakes a long overdue examination of the history of New York Public Service Law and documents the absence of legal support for the Commission's assertions of jurisdiction where upstream transactions are undertaken by entities which are not also operating companies." *Id.* at 510.

[28] The Abitibi Bowater settlement which Petitioners mention in their Additional Comments (at 14-16) involves direct expropriation, though there is nothing in Petitioners defense of their NAFTA claim that suggests they would be precluded from bringing any indirect expropriation claims to protect the interests of their investments.

does not offer the same U.S. Constitutional protections[29], and supercedes domestic law.[30]

A proper net benefits analysis as established in the Iberdrola decision requires consideration of benefits and countervailing risks or detriments properly attributable to the proposed transaction. A standard measure of legal risk for a class of events is R = probability of the event × the severity of the consequence. Such an evaluation must accept a reasonable degree of uncertainty as ambiguity or a lack of perfect information is an intractable part of risk management. As a result, extreme care should be taken in instances where possibilities, even remote, involve a major loss or other undesirable outcome. The Recommended Decision conflated uncertainty with risk when it stated that "Fortis's status as an investor from a NAFTA member state does not add any significant risk to the transaction." (RD at 46). There are ample and valid reservations about the conceivable and detrimental consequences of NAFTA investor rules which constitute both possible and plausible legal risk that should be recognized in considering if this merger should be permitted to proceed.

The ALJs solution to unanswered questions on NAFTA that "as a condition of the approval that Petitioners certify that no express promises have been made, extrinsic to this proceeding, that any particular regulatory treatment will be accorded Central Hudson or its parent company in the future" (RD at 46-47) is

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[29] *See generally* FPC v. Hope Nat. Gas Co., 320 U.S. 591 (1944); *see also* C. Austin, *NAFTA Regulatory Takings vs. Fifth Amendment Compensatory Rights: Tipping the Scales in Favor of Foreign Investment,* Currents: Int'l Trade LJ, 2004.

[30] *See* Been, V., & Beauvais, J. C., *The Global Fifth Amendment? NAFTA's Investment Protections and the Misguided Quest for an International 'Regulatory Takings' Doctrine,* NYUL Rev., 2003.

misplaced. What the ALJs seem to suggest is that they are searching for an indemnification against the exposure to NAFTA legal liability that this transaction entails. Despite its good intentions this effort is futile. Even if a foreign investor could contract away its right to avail itself to a NAFTA tribunal, such a contract imposed only on a corporate investor for having Canadian nationality signed under duress of a Commission threat to disapprove investment in a merger would likely violate the national treatment protections of NAFTA and be largely unenforceable. Allowing a Canadian company to takeover Central Hudson opens up a Pandora's box of NAFTA legal liability that has not been adequately addressed. The public interest would be better served if that box was left unopened and the transaction rejected by the Commission outright.

CONCLUSION

For the reasons stated, the proposed acquisition does not overcome the petitioners' burden and the Commission should reject this transaction outright. The proposed transaction as it currently stands is unequivocally not in the public interest. In line with the logic of the Recommended Decision no amount of tweaking or amplified positive benefit adjustments could salvage this merger at this point. Despite the justified apprehension by the ALJs in the Recommended Decision to reduce the public interest analysis to a mere "plebiscite", the proposed transaction has undeniably fomented massive public outcry and vehement opposition.

Central Hudson is a quintessential local utility. Many years ago it was caught up in the speculative financialization debacle of depression era utility holding

company pyramids, which ended under President Franklin Delano Roosevelt's reforms.[31] Since the 1940's, when Central Hudson was required by the SEC to be divested from the Niagara Hudson holding company, Central Hudson has remained a trusted local utility serving the needs of Main Street constituents. The Public Service Commission is the main institution in New York entrusted to ensure that statutory rules over regulated utilities are fairly applied and enforced. Nonetheless, the rationale behind encouraging public comment and widely disseminating opportunities for residential ratepayer input to filter into proceedings is to engender an open and inclusive regulatory process. If the Commission were to completely ignore the will of the people expressing sincere hesitation and instead imposed its own parochial notions of "public interest" the perceived injustice by many impassioned ratepayers who took the time to submit comments or attend public hearings risks tarnishing its storied reputation from that of a benevolent state body that crowd-sources community input in informing its decision-making process to one of a tyrannical autocrat shrouding itself in an empty veneer of citizen empowerment.

Utilities have been historically regulated in part to protect the universally cherished safe continuity of service on just and reasonable conditions, which generally requires a higher degree of risk aversion than private entities may normally entertain. This transaction is not only perceived by many to be inherently

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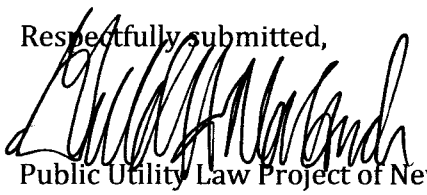
[31] *See generally* Public Utility Holding Company Act of 1935 (PUHCA), codified at that time at 15 U.S.C. § 79 et seq. PUHCA was repealed in 2005 in the Energy Policy Act of 2005, P.L. 109-58, 11 9 Stat. 594.

risky, but in fact leaves too much uncertainty and lingering questions regarding potential negative consequences. The emotional pleas by ratepayers in opposition of this merger, in addition to the concerns that the opposing parties have raised, is indicative of the general dissatisfaction with a proposal offering ephemeral putative benefits juxtaposed against unmitigated risks that endure and loom large.

PULP urges that this ill-conceived venture is treated with the same unrelenting disapproval and high degree of suspicion by the Commission that the Administrative Law Judges, numerous local governments, various public interest non-profits and community initiatives, and the ratepayers within the service area have already made resoundingly clear – reject this merger outright.

May 17, 2013

Respectfully submitted,



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