**UNITED STATES DISTRICT COURT**
**MIDDLE DISTRICT OF FLORIDA**
**JACKSONVILLE DIVISION**

**THE CITY OF JACKSONVILLE,**
**a State of Florida municipal corporation,**

**Plaintiff,**

**v.** **CASE NO.: 3:12-cv-850-J25-MCR**

**SHOPPES OF LAKESIDE, INC., a Florida corporation; JACKSONVILLE HOSPITALITY HOLDINGS L.P., a Delaware limited partnership; CONTINENTAL HOLDINGS, INC., a Wyoming Corporation,**

**Defendants,**
/

# REBUTTAL EXPERT REPORT OF SCOTT HEMPLING

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## I. Introduction

This Report responds to the Report of Douglas Branson, submitted on behalf of Defendant/Counter-Plaintiff, Continental Holdings, Inc. ("CHI") in the above-captioned case.

At issue is a 1943 transaction approved by the Securities and Exchange Commission ("SEC") under Section 11(e) of the Public Utility Holding Company Act of 1935 ("PUHCA," repealed 2005), and then ordered by a federal district court under that same provision. In the transaction, Jacksonville Gas Company ("Company"), a 50%-owned subsidiary of the American Gas and Power Company (a holding company registered under PUHCA), first formed Jacksonville Gas Corporation ("Corporation"). Company then transferred all of its assets and all of its liabilities (except certain first mortgage bonds, income debentures and income notes) to Corporation, which issued its new stock to Company's former major creditors. Company dissolved. Corporation—no longer owned by American Gas and Power Company—carried on the business formerly conducted by Company: manufacturing, distributing and selling gas to consumers in Jacksonville, Florida.

Mr. Branson asserts that the 1943 transaction "severed" the "chain" connecting Corporation to Company's predecessors, thereby preventing the transfer of CERCLA liability from Company to Corporation.[1]

I disagree with Mr. Branson. Congress enacted PUHCA to protect local public utility companies from the abuses arising from their control by complex holding company systems. Mr. Branson's fundamental error is to view a corporate disaffiliation required by PUHCA as an act of business severance, when PUHCA's explicit purpose was to ensure business continuity. In the case of the transaction between Jacksonville Gas Company and Jacksonville Gas Corporation, this purpose is confirmed by every fact available. My report organizes these facts according to two propositions.

1. Due to the very nature of PUHCA Section 11(e), the 1943 transaction has the characteristics of continuity in business activities, ownership and contracts that rebut any possibility of a broken chain. Indeed, the SEC described Corporation as having been "organized pursuant to the Plan *as successor to* Jacksonville Gas Company." *In the Matter of Jacksonville Gas Co*., 15 S.E.C. 74, 1943 WL 29724, at *1 (Dec. 27, 1943) (emphasis added).

2. Consistent with the purpose of business continuity, PUHCA Section 11(e) grants neither the SEC nor a court the power to make CERCLA liability disappear. Yet disappearance is precisely what flows from Mr. Branson's position, given that Company dissolved after transferring its business to Corporation.

My analysis demonstrates that the 1943 transaction could not, and did not, prevent the movement of CERCLA liability from Company to Corporation.

## II. Professional Background and Qualifications

My name is Scott Hempling. I am the President of Scott Hempling, Attorney at Law LLC. My business address is 417 St. Lawrence Drive, Silver Spring, Maryland 20901.

**Biographical background:** I began my legal career in 1984 as an associate in a private law firm, where I represented municipal power systems and others on transmission access, holding company structures, nuclear power plant construction prudence and producer-pipeline

[1] CERCLA refers to the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 ("CERCLA"), 42 U.S.C. §§ 9601 *et seq*. The statute was designed to promote the cleanup of hazardous waste sites and to ensure that cleanup costs are borne by those responsible for the contamination. *See, e.g*., *Burlington Northern v. U.S.*, 129 S. Ct. 1870, 1874 (2009).

gas contracts. From 1987 to 1990, I was employed by a public interest organization to work on electric utility issues. From 1990 to 2006, I had my own law practice, advising public and private sector clients—primarily state regulatory commissions, and also municipal systems, independent power producers, consumer advocates, public interest organizations and utilities—with an emphasis on electric utility regulation.

From October 2006 through August 2011, I was Executive Director of the National Regulatory Research Institute (NRRI). Founded by the National Association of Regulatory Utility Commissioners, NRRI is a Section 501(c)(3) organization funded primarily by state utility regulatory commissions. During my tenure, NRRI's mission was to provide research that empowered utility regulators to make decisions of the highest possible quality. As Executive Director, I was responsible for working with commissioners and commission staff at all 51 state-level regulatory agencies to develop and carry out research priorities in electricity, gas, telecommunications and water. In addition to overseeing the planning and publication of over 80 research papers by NRRI's staff experts and outside consultants, I published my own research papers, advised contract clients (including state commissions, regional transmission organizations, private industry and international institutions), and wrote monthly essays on effective regulation.

In September 2011, I returned to private practice, to focus on writing books and research papers, providing expert testimony, and teaching courses and seminars on the law and policy of utility regulation.

**Writing:** My book *Regulating Public Utility Performance: The Law of Market Structure, Pricing and Jurisdiction*, was published by the American Bar Association in 2013. This is the first volume of a two-volume treatise, the second of which will address the law of corporate structure, mergers and acquisitions. My book of essays, *Preside or Lead? The Attributes and Actions of Effective Regulators*, was published by NRRI in 2010. I published a second, expanded edition in 2013. I have written several dozen articles on utility regulation for publication in trade journals, law journals and books.

**Expert witness testimony:** I have testified many times on electric industry and public utility matters before Congressional and state legislative committees. As an expert witness I have testified before state administrative agencies, federal courts and arbitration panels. A list of my expert witness testimony and their dates appears on my resume attached to this report. I am being compensated for my services in this matter at a rate of $425.00 per hour.

**Teaching:** I am an Adjunct Professor at Georgetown University Law Center in Washington, D.C., where I teach two seminars: "Monopolies, Competition, and the Regulation of Public Utilities"; and "Regulatory Litigation: Roles, Skills and Strategies." In these seminars, students study the legal fundamentals in class, then apply that learning, under my supervision, in practicums at state and federal regulatory agencies. Since 1997, I have designed and taught commercial legal seminars on electricity law and public utility regulation to

thousands of students from all fifty states, from all professional disciplines relating to regulation (law, accounting, finance, economics, engineering) and from all regulated utility sectors.

**Speaking:** I have addressed hundreds of professional conferences throughout the United States and internationally. Domestic fora have included the American Bar Association, state-level bar associations, Federal Energy Bar Association, National Association of Regulatory Utility Commissioners, Massachusetts Institute of Technology, Yale Alumni in Energy, National Conference of Regulatory Attorneys; National Governors Association, Federal Energy Regulatory Commission, U.S. Department of Energy and U.S. Environmental Protection Agency. International fora have included the World Regulatory Forum, national regulatory agencies in India, Nigeria, New Zealand, Australia, Vanuatu, Jamaica, and Mexico; as well as universities in the United Kingdom, India and Germany; and associations of regulators in Canada and Italy.

**Clients:** My work as an advisor and litigator has focused on the public sector, where I have advised agencies or municipalities in approximately 25 states on matters relating to public utility regulation, in state agency proceedings, federal agency proceedings, and federal and state courts. As a subcontractor to the U.S. Department of State, I have advised the six nations of Central America on the regulatory infrastructure necessary to accommodate and encourage cross-national electricity transactions.

**Education and bar memberships:** I received a B.A. *cum laude* from Yale University in 1978, where I majored in (1) Economics and Political Science and (2) Music. I received a J.D. *magna cum laude* from Georgetown University Law Center in 1984. I am a member of the Bars of the District of Columbia and Maryland.

**Experience specific to PUHCA and corporate structure:** I have testified before the U.S. Senate four times and the U.S. House of Representatives four times on the subject of PUHCA and the corporate structure of utilities. I have represented clients who intervened in Securities and Exchange Commission proceedings on PUHCA matters involving mergers and acquisitions, interaffiliate transactions, and argued four PUHCA-related cases before the U.S. Courts of Appeals.

My resume is attached to this Report.

**Materials reviewed:** In preparing this Report, I reviewed the following materials:

- Mr. Branson's report;
- The Public Utility Holding Company Act of 1935;
- Jacksonville Gas Company's Certificate of Incorporation (July 28, 1927);
- Jacksonville Gas Company's "Submission of Plan" filed with the SEC in March 1942;

- *North Shore Gas Co. v. Salomon, Inc*., 152 F.3d 642, 651 (7th Cir. 1998);
- The SEC's Order of May 28, 1942 relating to this transaction;
- The U.S. District Court orders of May 29, 1942, Oct. 14, 1942 and Jan. 28, 1943 relating to this transaction;
- The SEC's submission to the U.S. District Court of Jan. 13, 1943;
- *In the Matter of Community Gas and Power Company, American Gas and Power Company and the Subsidiary Companies thereof*, Public Utilities Management Corporation, 13 S.E.C. 532, 1943 SEC LEXIS 1201 (July 2, 1943);
- *In the Matter of Jacksonville Gas Company and American Gas and Power Company*, 15 S.E.C. 74, 1943 WL 29724 (Dec. 27, 1943);
- Brown's Directory of American Gas Companies for the years 1942, 1943-44 and 1944-45;
- *In re Community Gas and Power Co*., 168 F.2d 740 (3d Cir. 1948);
- Amendment Nos. 1-6 of Company's Section 11(e) Application to the SEC;
- *In re Jacksonville Gas Co*., 46 F.Supp. 852 (S.D. Fla. 1942);
- Amendment Nos. 7-10 of Company's Section 11(e) Application to the SEC (ultimately approved by the District Court);
- Order for hearing of the Securities and Exchange Commission dated November 13, 1942;
- Supplemental Order of the Securities and Exchange Commission dated December 8, 1942;
- Second Supplemental Order of the Securities and Exchange Commission dated January 8, 1943;
- Corporation's actual Certificate of Incorporation filed with the Florida Secretary of State on Feb. 1, 1943; and
- Document No. 114838 (May 16, 1946) on file with the Florida Secretary of State (recording Company's dissolution); and
- Any other materials cited herein.

## III. PUHCA's purpose: Protect investors, consumers and the public by limiting utility holding companies to a single integrated public-utility holding company system

Enacted in 1935, PUHCA[2] required, subject to certain exceptions, that each utility holding company constitute a "single integrated public-utility system."[3] Congress sought to

[2] 15 U.S.C. sec. 79 *et seq.* (repealed 2005).

[3] Section 2(a)(29)(B) of PUHCA defined "integrated public-utility system," as applied to gas utility companies, to mean—

> a system consisting of one or more gas utility companies which are so located and related that substantial economies may be effectuated by being operated as a

protect investors and consumers from abuse, by simplifying corporate structure, requiring conservative financing, reducing the presence and influence of risky non-utility businesses, all with the purpose of aligning each utility's corporate form with its public service obligations. While the Act had many complex provisions, the key tools were these:

> Section 11(b)(1) required the SEC to break up holding company systems that owned scattered utility companies and unrelated businesses so that, after the break-ups, each system would be confined to a single "integrated public-utility system," subject to certain exceptions.
>
> Section 10(b)(1) required the SEC to disapprove any acquisition by a utility holding company if the acquisition would "tend towards ... concentration of control of public-utility companies, of a kind or to an extent detrimental to the public interest or the interest of investors, or consumers."
>
> Section 10(c)(2) allowed only those acquisitions that "tended towards the economic and efficient development of an integrated public-utility system."
>
> Section 7(d) prohibited utility holding companies from issuing securities that, among other things, involved an "improper risk" or were "detrimental to the public interest or the interest of investors or consumers."

For 70 years, these provisions caused electric and gas utilities to "stick to their knitting": to devote their management attention and financial resources to providing essential utility service, locally. The "integrated system" principle eliminated or limited those features of holding company structure and behavior that cause harm to investors, consumers and the public interest: geographic dispersion of utility properties, arbitrary (from a consumer perspective) mixtures of utility and non-utility businesses, layers of corporate affiliates, excess debt leveraging, utility financial support of non-utility businesses, and interaffiliate transactions priced unfairly to consumers. In a sentence, the "integrated system" principle prevented acquisitions for the sake of acquisitions—acquisitions motivated by "strategy" rather than economies and efficiencies.

To enforce the "integrated system" principle, the Securities and Exchange Commission, beginning in 1935, broke up the then-existing 13 holding companies into several hundred

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> single coordinated system confined in its operations to a single area or region, in one or more States, not so large as to impair (considering the state of the art and the area or region affected) the advantages of localized management, efficient operation, and the effectiveness of regulation: Provided, That gas utility companies deriving natural gas from a common source of supply may be deemed to be included in a single area or region.

relatively local systems. (Some multi-state systems remained, in a form called "registered holding companies" that were subject to extra regulatory oversight).

## IV. The 1943 transaction has the prerequisites for preserving successor liability

Mr. Branson, either explicitly or implicitly, argues that the 1943 transaction did not preserve successor liability because it was neither a *de facto* merger nor a continuation of an existing business. I disagree. This transaction occurred within the context of PUHCA—a statute whose purpose was to detach a vulnerable public utility from unrelated business activities so that it can continue as an existing business—here, the business of manufacturing, distributing and selling gas to consumers in Jacksonville. By failing to consider the PUHCA context, and by disregarding relevant facts, Mr. Branson comes to the wrong conclusion.

### A. Section 11(e)'s purpose: Simplify the structure and continue the public utility business

PUHCA Section 11(e) requires that a simplification plan be designed to enable a company to "comply with the provisions of section 11(b)." The purpose of Section 11(b) is to limit each utility holding company system to "a single integrated public-utility system, and to such other businesses as are reasonably incidental, or economically necessary or appropriate to the operations of such integrated public-utility system."[4]

Because the statutory goal is a "single integrated public-utility system, a Section 11(e) transaction is necessarily a reorganization—specifically, a reorganization of one or more existing utility businesses. *See North Shore Gas Co. v. Salomon, Inc*., 152 F.3d 642, 651 (7th Cir. 1998) (explaining that in a Section 11(e) transaction, what is being reorganized is "a single business enterprise").[5] In this context, the purpose of reorganization is to simplify—to allow a utility business formerly controlled by a holding company embodying PUHCA Section 1's "evils" to exist and operate free of that control. In such a transaction, "identity between what entered the transaction and what emerged from it is much more likely than in an asset sale between strangers." *Id*. As I will detail next, this statutory purpose—to preserve and continue a

[4] PUHCA Section 11(b)(1). This "single integrated public-utility system" requirement is subject to an exception described in PUHCA Section 11(b)(1)(A), (B) and (C) and not relevant here.

[5] *North Shore Gas* was overruled by *Envision Healthcare, Inc. v. PreferredOne Ins. Co.*, 152 F.3d 642 (7th Cir. 2010). The basis for the overruling was unrelated to PUHCA or successor liability. The basis for the overruling was the standard of review by an appellate court of district court decisions on declaratory orders. In my view, none of the propositions for which my report cites *North Shore Gas* are rendered less persuasive by this overruling.

viable public utility company service—is exemplified by the design and implementation of the 1943 Plan.

### B. The 1943 transaction was designed to ensure that Company's business would be continued by Corporation

The purpose of a simplification plan under PUHCA is to continue the existing utility businesses, free of the distractions and abuses arising from affiliation with complex holding company systems.[6] The SEC here pursued that purpose by recognizing and ensuring three things: continuity of the business activities, continuity of ownership and continuity of contracts.

**1. Continuity of the business activities:** In valuing the business for purposes of reorganization, the SEC determined "the earning power of the enterprise." SEC Order of May 28, 1942 at 11-13. To do so, it assembled Company's financial data for the years 1936 through 1941. From that factual foundation it estimated future earnings, capitalizing them at 8% to arrive at a present value of $2.625 million. *Id.* at 13. Using past financial performance to project future income, and from that projection to compute present value, makes sense only when the purpose is to continue the business. The SEC recognized this continuity when it described Corporation as having been "organized pursuant to the Plan *as successor to* Jacksonville Gas Company."[7]

The continuity from Company to Corporation is also made clear by comparing editions of *Brown's Directory of American Gas Companies* for the years 1942, 1943-44 and 1944-45. The 1942 edition lists Company as the gas firm supplying Jacksonville. The 1943-44 and 1944-45 editions list Corporation in the same page position that Company had occupied (with Company gone). In all three editions, the address (29 E. Adams St.) and President and General Manager (A. F. Traver) are the same. Also the same, in all three editions, are statements that the firm "supplies Jacksonville and South Jacksonville" and has "one retail store." And also similar, in all three editions, are facts about the gas manufacture process, heavy oil use, annual

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[6] That American Gas and Power Company required reorganization is evident from its structure. Above American in its holding company system was Community Gas and Power Company, which owned 18.38% of American's common stock. Together these two holding companies owned another holding company and seven subsidiary operating companies, located in Florida, Maine, Minnesota, Massachusetts, Alabama and Georgia. *See In the Matter of Community Gas and Power Company, American Gas and Power Company and the Subsidiary Companies thereof, Public Utilities Management Corporation*, 13 S.E.C. 532, 1943 SEC LEXIS 1201 (July 2, 1943).

[7] *In the Matter of Jacksonville Gas Company and American Gas and Power Company*, 15 S.E.C. 74, 1943 WL 29724 at *1 (Dec. 27, 1943) (emphasis added).

production, by-products made, miles of mains, number of services in the ground, and annual sales.[8]

**2. Continuity of ownership:** The 1943 Plan called for Corporation to issue its new stock not to Company's stockholders, but to Company's major creditors. Did this feature "break the chain" between Company and Corporation? No, because of a key finding made by the SEC. The SEC found that Company's stated equity—only 10.77% to begin with—was an exaggeration due to "inflated" asset values on Company's books. What the stockholders actually owned, the SEC found, was—nothing. "[T]he stock of the company has no possible equity in the enterprise." SEC Order of May 28, 1942 at 3. Stock ownership gives voting power, but in this situation that voting power was "an incident of stock without equity." *Id*. at 8. Under these circumstances, transferring ownership to the creditors was a statutory necessity, to satisfy Section 11(a)'s requirement that "voting power [be] fairly and equitably distributed among the holders of securities…".

Mr. Branson appears to view this transfer of ownership, from Company's equity-less stockowners to its creditors, as a break in continuity. But the SEC, honoring PUHCA Section 11, intended the opposite. The SEC viewed Company as *already being owned by its creditors.* Thus the issuance of Corporation stock to Company's creditors, while technically a transfer of ownership, was actually a *recognition* of ownership. Given the "absence of value in the common stock," the SEC found, Company's own plan "proceeds on the assumption that the enterprise *belongs to and should be controlled by the company's creditors*." SEC Order May 28, 1942 at 3 (emphasis added).

The purpose of technically transferring ownership, therefore, was not to change the nature of the business but to recognize the reality of the business—and to fix the inequitable distribution of voting power deemed unlawful by the SEC. The goal was not to change the utility business but to save it; not to break a chain, but to ensure continuity in the chain. The goal was not to "disrupt" continuity but to comply with Section 11(b)(2), by eliminating features of Company's and American's corporate structure that "unduly or unnecessarily complicate[d] the structure, or unfairly or inequitably distribute[d] voting power among security holders." The purpose was "to effectuate a divorcement of the new corporation from control by American," SEC Order of May 28, 1942 at 27; the purpose was not to effect a divorcement of Corporation's obligations from Company's obligations. The business of Company would be continued by Corporation, henceforth unhindered by affiliation with American Gas and Power Company.

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[8] Two unsurprising changes were that by 1944-45 (1) "management" was "independent," *i.e.*, no longer performed by the affiliated Public Utilities Management Corporation; and (2) common stock was held publicly. Both these factors result from Jacksonville Gas Corporation becoming independent of the holding company American Gas and Power Company.

**3. Continuity of contracts:** Ordinary contracts for supply and materials would be maintained; all others would be terminable by Corporation's new board. SEC Order of May 28, 1942 at 5. The existing services agreement with the affiliated Public Utilities Management Corporation—a source of SEC concern (payments made by Company to it for services "may have been excessive, or some of the services may have been unnecessary," SEC Order of May 28, 1942 at 13, would terminate automatically on a date defined by the SEC. *Id.* at 28.

**4. What about Continuity of management and board?** "The plan provides for no immediate change in the management of the new company…." SEC Order of May 28 at p.5. But a change in management would have been likely: "[N]ew stockholders will have a management of their own choosing," because present management will "have no right .... to nominate any candidate for election to the new board...". *Id*. at 27-28. As for board membership, Corporation's initial board will consist of the directors of Company's board. That board can nominate candidates, but so can the new shareholders. SEC Order of May 28, 1942 at 5. Based on these statements, I readily acknowledge that Corporation could end up with management and board members different from Company's.

But, my acknowledgment is of no moment because, in a Section 11(e) reorganization, changes in management and board composition should come as no surprise. Such changes will be necessary to protect the utility from control by individuals who themselves were controlled by a holding company system displaying the "evils" that PUHCA was enacted to eliminate. And the SEC expressly found that Company was afflicted by four of those evils, each described vividly in the statute:

1. PUHCA Section 1(b)(3): Control of utility companies was being "exerted through disproportionately small investment." The SEC found that, for Company, the voting power was in capital stock whose underlying capital and surplus accounts, "on the basis of any realistic statement of the company's assets, would show a substantial deficit." SEC Order of May 28, 1942 at 3. *See also id*. at 8 (requiring that "the voting power attach to a security which represents a real equity in the company").

2. PUHCA Section 1(b)(1): Securities were being "issued upon the basis of fictitious or unsound asset values having no fair relation to the sums invested in or the earning capacity of the properties." The SEC found that Company's "plant account [has not] borne any reasonable relationship to the cost or value of its properties"; and that its "debt structure, erected on the basis of the inflated plant account, has imposed interest requirements far in excess of the earning power of the company." SEC Order of May 28, 1942 at 2.

3. PUHCA Section 11(b)(2): Corporate structures "unfairly or inequitably distribute[d] voting power among security holders." The SEC found that the voting power in Company was held by the holders of stock that "has no possible

equity in the enterprise," and is "distributed unfairly and inequitably among security holders." SEC Order of May 28, 1942 at 3.

4. PUHCA Section 1(b)(2): Utility companies were being "subjected to excessive charges for services, construction work, equipment, and materials," or were "enter[ing] into transactions in which evils result from an absence of arm's length bargaining or from restraint of free and independent competition." The SEC stated that "payments made [by Company] to Public Utilities Management Corporation [an affiliate of Company and its holding company owner] for accounting, secretarial, engineering and other services rendered by it may have been excessive, or some of the services may have been unnecessary." SEC Order of May 28, 1942 at 13.

Since these problems likely arose due to decisions by Company's management and board (likely directed, in turn, by the ultimate holding company and its board), there should be no expectation that existing management and board would continue, in this instance or in any Section 11(e) transaction. A discontinuity in holding company-controlled management and board would assist the continuity of the business.

The aforementioned continuity factors—business activities, ownership and contracts—should not surprise, because the 1943 transaction was a reorganization of an existing business, not the severance of a new business from an existing business. "[W]hen an asset purchase is more properly described as a reorganization, the 'purchaser' will find it difficult to escape liability, because one or more of the successor liability exceptions will suggest that the seller has survived the sale." *North Shore Gas*, 152 F.3d at 651. *See also id.* at 653-54 ("[I]n the context of a Holding Company Act reorganization and CERCLA, the policy of the de facto merger exception must find application here....[O]ur overall analysis is strongly buttressed by the fact that the Gas Company *continued all the utility aspects* of the Coke Company's operations.") (emphasis added).

### C. Mr. Branson's "broken chain" theory is contradicted by the facts

Mr. Branson states that "[u]nder the plan, a new entity, Jacksonville Gas Corporation (not Company) succeeded to the assets and certain of the liabilities of the Jacksonville Gas Company." Report at para. 30. He later adds:

> Company's shareholders surrendered their 50,000 plus common shares, receiving nothing in return. Instead of an issuance of stock to shareholders of the old company, the new Jacksonville Gas Corporation issued all common shares to the creditors of the old company, mainly the holders of three classes of debt securities.

*Id.* at Para. 34. Based on these facts, Mr. Branson characterizes the plan as "a stock for assets transaction rather than a merger" (and, presumably, not the continuation of a business).

Mr. Branson's conclusion is wrong because he ignores the key fact I just discussed: Corporation's new shares went to Company's creditors rather than its shareholders -- because what Company's shareholders owned was, literally, nothing. They owned stock unsupported by equity. Given this fact, the SEC found that *Company's creditors had already become the owners of Company before Company transferred its business to Corporation.* The issuance of Corporation stock to the creditors thus recognized reality: The real economic interest in the business rested with the creditors, not the shareholders. To view the chain of ownership as "severed or broken" disregards that reality.

Confirming Mr. Branson's error is another error in his Report. He states (Report at para. 34) that "[a]ny unassumed liability would have remained with the selling entity." This statement also ignores reality, because "upon transfer and distribution of all of its assets, the company would surrender its charter and be dissolved." SEC Order of March 28, 1942 at 4. Liability could not have "remained" with a company that dissolved.

Mr. Branson's view, that the transaction was merely "stock for assets," is an interpretation unsupported by the facts. Here are the relevant facts: Corporation's Certificate of Incorporation states that Corporation will "acquire the assets of Jacksonville Gas Company in accordance with the plan to effectuate the provisions of Section 11(b) of the Public Utility Holding Company Act of 1935 approved by the Securities and Exchange Commission by its order made May 28, 1942."[9] The business that Corporation intended to engage in was this:

> To acquire, buy, hold, own, sell, lease, exchange, dispose of, finance, deal in, construct, build, equip, improve, use, operate, maintain and work upon:
>
> > (a) any and all kinds of plants and systems for the manufacture, storage, utilization, supply, distribution, transmission or disposition of gas, light, heat, power, refrigeration, water or ice;
> >
> > (b) any and all kinds of works, plants, substations, systems, pipe lines, tracks, machinery, apparatus, devices, supplies, and articles of every kind pertaining to or in any wise connected with the manufacture, purchase,

[9] Corporation was incorporated on Feb. 1, 1943. *See* Certificate of Incorporation of Jacksonville Gas Corp., as filed in Ofc. of Sec. of State of Fla., Feb. 1, 1943 ("Jacksonville Gas Corporation Certificate of Incorporation"). *See also* Exhibit "Y" to Amendment No. 7 of Company's Section 11(e) Application to the SEC (ultimately approved by the District Court); *see also Brown's Directory of American Gas Companies*, 1943-44 Edition at 47.

> use, distribution, regulation, control or application of gas, light, heat, power, refrigeration, water or ice.
>
> […]
>
> To buy or otherwise obtain, to produce, to hold, own, sell, dispose of, distribute, deal in, use, furnish and supply gas of every form, whether artificial or natural, light, heat, power, refrigeration, water and ice.[10]

This is precisely the business that Company had engaged in.[11] Corporation then proceeded to engage in the very business its Certificate of Incorporation said it would: operating plants and systems for the manufacturing and selling of gas in Jacksonville.[12]

### D. Mr. Branson ignores language confirming Corporation's express assumption of Company's liability

In approving the Plan, the SEC determined that "[t]he new corporation [Corporation] would acquire all the assets of the present company [Company] and would assume *all of its liabilities* except the *presently outstanding* first mortgage bonds, income debentures and income notes." SEC Order of May 28, 1942 at 3 (emphasis added). Notice the placement of the term "presently." The Plan applies a temporal limitation ("presently") to the specified financial liabilities but imposes *no such temporal limitation* to "all" the other liabilities. This key distinction was repeated by the District Court, when it directed Company to "[c]ause Jacksonville Gas Corporation to assume *all of the liabilities* of Jacksonville Gas Company, except the *presently outstanding* first mortgage bonds, income debentures and income notes of Jacksonville Gas Company...." October 14, 1942 Order at 4 (emphasis added). The absence of a temporal limitation on the non-financial liabilities, adjacent to the use of such a limitation on the financial liabilities, compels a conclusion that CERCLA liability moved from Company to Corporation.

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[10] Certificate of Incorporation of Jacksonville Gas Corporation at second paragraph.

[11] *See* Certificate of Incorporation of Jacksonville Gas Co., dated July 28, 1927, at p. 1, ¶ 1(a) & (b) (containing substantially similar language as above, excluding the term “water”); *see also* SEC Order of May 28, 1942 at 3 (describing Company as a "public utility company which owns and operates a manufactured gas plant, ... and a manufactured gas transmission and distribution system," in the Jacksonville area).

[12] *See, e.g., Jacksonville Gas Corp. v. Florida Railroad and Public Utilities Commission*, 50 So.2d 887 (Fla. 1951) (reviewing retail gas rates charged by Corporation in Jacksonville).

Nowhere does Mr. Branson address this language. While persuasive on its own, its significance is confirmed by the Seventh Circuit's decision in *North Shore Gas*. There the reorganization plan provided that the receiving corporation "shall assume *liabilities and obligations of every kind and character . . . accrued to or existing on the date of transfer.*" 152 F.3d at 652 (emphasis in court's opinion). The Seventh Circuit noted that "[t]he use of the word "existing" "fairly obviously forecloses the possibility that [the purchaser] agreed to assume any contingent liabilities, much less the environmental liabilities at issue here." *Id*. (quoting other authorities). The Seventh Circuit then went on, however, to find that the de facto theory of successor liability in fact applied, and imposed successor liability under CERCLA on the receiving corporation. In the Jacksonville situation, there is no need to apply the de facto analysis because the contrasting language ("presently outstanding" vs. "all") requires a finding of express assumption of liability by Corporation.

In summary, a Section 11(e) transaction is a reorganization—a reorganization of an existing business designed to preserve the continuity of that business.[13] And "when an asset purchase is more properly described as a reorganization, the "purchaser" will find it difficult to escape liability, because one or more of the successor liability exceptions will suggest that the seller has survived the sale." *North Shore Gas*, *supra,* 152 F.3d at 651.

## V. PUHCA Section 11(e) grants neither the SEC nor a court the power to make tort liability disappear

### A. PUHCA transactions do not affect tort liability

Mr. Branson states (at para. 37) that a "Plan of Simplification [under PUHCA Section 11(e)] deals with capital and corporate structure: it has nothing to do with assumption *vel non* of tort liability." His statement is correct. Tort liability is not within the SEC's PUHCA jurisdiction. Consequently the Plan proposed by Company in March 1942, the SEC orders, the SEC's proposal to the federal court and the court's decision cannot be viewed as affecting tort liability.

Mr. Branson sees it differently. From his correct assertion—that a PUHCA simplification plan does not deal with tort liability—he draws an incorrect conclusion—that the Plan ensured Corporation's non-liability. Both PUHCA and the Plan have the same purpose: to continue the Company's business free of the risks arising from its affiliation with American Gas and Power Company. The SEC would have no reason, or jurisdiction, to put its imprimatur on

[13] *See In re Community Gas and Power*, 168 F.2d 740 (3d Cir. 1948) (holding that "a reorganization under the Public Utility Holding Company Act normally involves the reorganization of a going solvent business which is destined to continue rather than the liquidation and winding up of an enterprise which is terminating").

a plan that determined tort liability or affected its migration from Company to Corporation based on legal principles outside of PUHCA.

Mr. Branson's conclusion runs into another contradicting fact: Company's dissolution. If Company liability did not pass to Corporation, it would have disappeared, because Company dissolved by design of the Plan: "[U]pon transfer and distribution of all of its assets, the company would surrender its charter and be dissolved." SEC Order of May 28, 1942 at 4.[14] So the necessary effect of Mr. Branson's insistence on Corporation's non-liability is to impute to the SEC (and to PUHCA) an intent that PUHCA-mandated reorganizations can extinguish tort liabilities. Mr. Branson would read an anti-public interest intent into a statute with an explicit public interest purpose. Such a reading has no basis in law, policy, logic or fact.

### B. The absence of tort liabilities on the Company's 1942 balance sheets does not mean they disappeared when the transaction occurred

Mr. Branson notes that on Company's balance sheet (as presented in the SEC orders and court orders) there is no reference to tort liability. Para. 39. He then states that "[b]y contrast, balance sheet Note C[15] does disclose a contingent liability for a possible future contract claim." Para. 40. From these facts, he concludes that "[w]ere any assumption of tort liabilities by the emerging entity to have been contemplated, the balance sheet would have set up reserves for known liabilities, and made footnote disclosure for contingent liabilities." *Id.*

I disagree. Mr. Branson's is using a balance sheet whose purpose is to display known financials to draw a conclusions about unknown liabilities. His related error assumes that, by including in its Order a balance sheet that mentioned no tort liabilities, the SEC intended (given that the Plan included Company's dissolution) to extinguish those liabilities. As I explained in Part V.A, such an assumption has no basis in law, policy, logic or fact. A company cannot escape its tort liability by forming a new company and then dissolving:

> Congress [in enacting CERCLA] was unlikely to leave a loophole that would enable corporations to die "paper deaths, only to rise phoenix-like from the ashes, transformed, but free of their former liabilities."

*North Shore Gas Co*., *supra,* 152 F.3d at 649 (quoting other authorities).

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[14] A corporate record on file with the Florida Secretary of State shows that Company was "dissolved by proclamation." Florida Department of State, Division of Corporations, Document No. 114838 (May 16, 1946).

[15] Sic. The contract contingency is described in Note B.

Mr. Branson also asserts (para. 41) that "modern practice [in balance sheets, I assume] is to treat contractual liabilities and obligations separately from possible tort claims." He does not say whether that "modern practice" applied in 1942. And he severs these balance sheets from their context. The context is that the Company was reorganized solely to satisfy PUHCA, so the purpose of the balance sheets is to reflect financial assets accurately, then use corporate reorganization to rearrange those assets to satisfy Section 11's command that "voting power [be] fairly and equitably distributed among the holders of securities" in a "single integrated public-utility system." In this context, the absence from the balance sheet of tort-relevant information is unremarkable.[16] The PUHCA purpose for these financial statements was solely to disclose financial facts, not to assign or eliminate tort liability. Whatever liability Corporation acquired or did not acquire will depend on legal sources other than PUHCA.

In a passage not cited by Mr. Branson, the SEC held that "[c]ertain other persons having preferred or general claims against the company were not affected by the plan inasmuch as the new company will assume the obligations of the old company to such persons and their claims against the new company will be at least as good as their claims against the present company." SEC Order of May 28, 1942 at 9. It is not clear whether this sentence relates only to financial stakeholders whose interests were not explicitly protected by the Plan, or instead to all possible claimants (such as future tort claimants). If this sentence includes tort claimants, then we have explicit support for Corporation's liability (to the extent Company was liable). And if this sentence refers only to bondholders, my previous reasoning still applies: A Section 11(e) plan cannot eliminate tort liability.[17]

To support his position that the Plan eliminated tort liability, Mr. Branson (at para 36) cites the change in language from Company's proposal of March 21, 1942 to the SEC's order of May 28, 1942. The Company-proposed plan said Corporation would "assume all its [i.e., Company's] debts of every kind and character." The SEC approval order said that Corporation would "assume all of the liabilities" of [Company]. Mr. Branson focuses on the disappearance of the phrase "of every kind and character." The language does differ, but the difference undermines Mr. Branson's opinion, because the SEC's "liabilities" is broader than the Company's "debts." And since "all" means "all," the SEC's "all" is no less expansive than Company's "of every kind and character." So even if one were to assume that the term

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[16] This is assuming the authors of the plan had such information. Because if they lacked the information, they would have no duty to disclose; and if they had the information but failed to disclose it, that failure could hardly affect whether the liability transferred to Corporation.

[17] *Cf. North Shore Gas*, *supra,* 152 F.3d at 658 ("We fail to see why a plan of reorganization—undertaken only to ensure compliance with the Holding Company Act and to resolve other structural and financial issues—should act as a firewall that effectively extinguishes the Coke Company's direct CERCLA liability").

"liabilities" in a Section 11(e) document would include tort liabilities, the SEC's language actually signals their transfer to Corporation, contrary to Mr. Branson's assumptions.

## VI. Conclusion

The 1943 transaction was a reorganization. It was designed to comply with PUHCA's mandate that each public utility be part of a "single integrated public-utility system." Proposed by Jacksonville Gas Company, approved by the SEC, and ordered by the U.S. District Court, the Plan was crafted to cause Company's gas business to continue in the hands of its SEC-approved successor, Corporation. Company's major creditors became Corporation's owners because the SEC deemed those creditors to have already become Company's owners, given the absence of any equity underlying the stock held by Company's nominal owners. This combination of PUHCA purpose and ownership reality means that Mr. Branson's claim of "broken chain" has no basis in fact.

Nor has it any basis in logic. To infer a broken chain from these facts is to grant the SEC the power it did not have—the power to erase tort liabilities. Here, the SEC approved a plan that included Company's dissolution. So if a Company tort liability did not go to Corporation it would have disappeared. PUHCA granted the SEC large powers, but eliminating tort liability was not one of them.

Not only was there no broken chain preventing liability to transfer; there was express intent that liability would transfer. What moved from Company to Corporation, along with business activities, ownership and contracts, was "all" liabilities: all liabilities, that is, except for certain of Company's "presently outstanding" indebtedness. By excepting a class of liabilities that was temporally limited (by the phrase "presently outstanding") but including a class that was not thus limited, the SEC-approved, court-approved Plan transferred to Corporation whatever CERCLA liability would otherwise lie with Company.

Dated:

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Scott Hempling
Scott Hempling, Attorney at Law LLC

## Scott Hempling, Attorney at Law

Scott Hempling is an attorney, expert witness and teacher. As an attorney, he has assisted clients from all industry sectors—regulators, utilities, consumer organizations, independent competitors and environmental organizations. As an expert witness, he has testified numerous times before state commissions and before committees of the United States Congress and the legislatures of Arkansas, California, Maryland, Minnesota, Nevada, North Carolina, South Carolina, Vermont, and Virginia. As a teacher and seminar presenter, he has taught public utility law and policy to a generation of regulators and practitioners, appearing throughout the United States and in Canada, Central America, Germany, India, Italy, Jamaica, Mexico, New Zealand, Nigeria and Peru.

The first volume of his legal treatise, *Regulating Public Utility Performance: The Law of Market Structure, Pricing and Jurisdiction*, was published by the American Bar Association in 2013. It has been described as a "comprehensive regulatory treatise [that] warrants comparison with Kahn and Phillips." The second volume will address the law of corporate structure, mergers and acquisitions. His book of essays, *Preside or Lead? The Attributes and Actions of Effective Regulators*, has been described as "matchless" and "timeless"; a Spanish translation will be widely circulated throughout Latin America, through the auspices of the Asociación Iberoamericana de Entidades Reguladoras de la Energía and REGULATEL (an association of telecommunications regulators from Europe and Latin America). The essays continue monthly at www.scotthemplinglaw.com.

His articles have appeared in the *Energy Bar Journal*, the *Electricity Journal*, *Energy Regulation Quarterly, Public Utilities Fortnightly*, *ElectricityPolicy.com*, publications of the American Bar Association, and other professional publications. These articles cover such topics as mergers and acquisitions, the introduction of competition into formerly monopolistic markets, corporate restructuring, ratemaking, utility investments in nonutility businesses, transmission planning, renewable energy and state–federal jurisdictional issues. From 2006 to 2011, he was the Executive Director of the National Regulatory Research Institute.

Hempling is an adjunct professor at the Georgetown University Law Center, where he teaches courses on public utility law and regulatory litigation. He received a B.A. *cum laude* in (1) Economics and Political Science and (2) Music from Yale University, where he was awarded a Continental Grain Fellowship and a Patterson research grant. He received a J.D. *magna cum laude* from Georgetown University Law Center, where he was the recipient of an *American Jurisprudence* award for Constitutional Law. Hempling is a member of the U.S. Department of Energy's Future Electric Utility Regulation Advisory Group. More detail is available at www.scotthemplinglaw.com.

## Education

B.A. *cum laude*, Yale University (majors: Economics and Political Science, Music), 1978. Recipient of a Continental Grain Fellowship and a Patterson Research grant.

J.D. *magna cum laude*, Georgetown University Law Center, 1984. Recipient of *American Jurisprudence* award for Constitutional Law; editor of *Law and Policy in International Business*; instructor, legal research and writing.

## Professional Experience

President, Scott Hempling, Attorney at Law LLC (2011–present)

Adjunct Professor, Georgetown University Law Center (2011–present)

Executive Director, National Regulatory Research Institute (2006–2011)

Founder and President, Law Offices of Scott Hempling, P.C. (1990–2006)

Attorney, Environmental Action Foundation (1987–1990)

Attorney, Spiegel and McDiarmid (1984–1987)

## Past Clients

**Independent Power Producers and Marketers**

California Wind Energy Association, Cannon Power Company, Electric Power Supply Association, EnerTran Technology Company, National Independent Power Producers, SmartEnergy.com, U.S. Wind Force.

**Investor-Owned Utilities**

Madison Gas & Electric, Oklahoma Gas & Electric.

**Legislative Bodies**

Vermont Legislature, South Carolina Senate.

**Municipalities and Counties**

Connecticut Municipal Electric Energy Cooperative; Iowa Association of Municipal Utilities; City of Jacksonville, Florida; City of Winter Park, Florida; Montgomery County, Maryland; American Public Power Association.

**Public Interest Organizations**

Alliance for Affordable Energy, American Association of Retired Persons, Consumer Federation of America, Energy Foundation, Environmental Action Foundation, GRID2.0 (Washington, D.C.), Illinois Citizens Utility Board, Union of Concerned Scientists.

**Regulatory Commissions and Consumer Agencies**

Arkansas Public Service Commission, Arizona Corporation Commission, Connecticut Department of Public Utility Control, Connecticut Office of Consumer Counsel, Delaware Public Service Commission, Hawaii Public Utilities Commission, State of Hawaii Office of Planning, Indiana Utility Regulatory Commission, Kansas Corporation Commission, State of Maryland, Maryland Energy Administration, Maryland Attorney General, Maryland Office of People's Counsel, Massachusetts Attorney General, Massachusetts Department of Public Utilities, Mexico's Comisión Reguladora de Energía, Minnesota Public Utilities Commission, Mississippi Public Service Commission, Mississippi Public Utilities Staff, Missouri Public Service Commission, Montana Public Service Commission, National Association of Regulatory Utility Commissioners, Nevada Consumer Advocate, Nevada Public Service Commission, New Hampshire Public Utilities Commission, New Jersey Division of Ratepayer Advocate, North Carolina Utilities Commission, Ohio Public Utilities Commission, Oklahoma Corporation Commission, Pennsylvania Office of Consumer Advocate, Puerto Rico Energy Commission, South Carolina Public Service Commission, Texas Office of Public Utility Counsel, Vermont Department of Public Service, Virginia State Corporation Commission, Wisconsin Attorney General.

## Testimony Before Legislative Bodies

**United States Senate**

Committee on Energy and Natural Resources, May 2008 (addressing the adequacy of state and federal regulation of electric utility holding company structures).

Committee on Energy and Natural Resources, Feb. 2002 (analyzing bill to amend the Public Utility Holding Company Act) (PUHCA).

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**United States House of Representatives**

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Subcommittee on Energy and Power, Energy and Commerce Committee, July 1994 (analyzing future of the electric industry).

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Subcommittee on Environment, Energy and Natural Resources, Government Operations Committee, Oct. 1990 (assessing electric utility policies of FERC).

Appropriations Subcommittee on Commerce, Justice, State and the Judiciary, Apr. 1989 (discussing proposals to increase staff administering PUHCA).

Subcommittee on Energy and Power, Sept. 1988 (discussing "independent power producers" and PUHCA).

**State Legislatures**

Judiciary Committee, South Carolina Senate (2000) (discussing options for introducing retail electricity competition).

Commerce Committee, Arkansas General Assembly (1999) (discussing legislation to introduce retail electricity competition).

Health Access Oversight Committee, Vermont General Assembly (1999) (discussing options for state regulation of prescription drug pricing).

Electricity Restructuring Task Force, Virginia General Assembly (1999) (discussing options for introducing retail electricity competition).

Study Committee, North Carolina Legislature (1999) (discussing legislation to introduce retail electricity competition).

Committees on General Affairs, Finance, Vermont Senate (February-March 1997) (discussing options for structuring the electric industry).

Task Force to Study Retail Electric Competition, Maryland General Assembly (1997) (discussing options for introducing retail electricity competition).

Interim Committee on Electric Restructuring, Nevada Legislature (1995-97) (discussing options for structuring the electric industry).

Committee on Energy and Public Utilities, California Senate (December 1989) (discussing relationships between electric utilities and their non-regulated affiliates).

## Testimony Before Commissions, Courts and Arbitration Panels

New Jersey Board of Public Utilities: Transfer of utility transmission assets to holding company affiliate (2015-2016).

Hawaii Public Utilities Commission: Holding company acquisition of utility holding company (2015-2016).

Louisiana Public Service Commission: Holding company acquisition of utility holding company (2015).

Connecticut Public Utilities Regulatory Authority: Holding company acquisition of utility holding company (2015).

District of Columbia Public Service Commission: Holding company acquisition of utility holding company (2014-15).

Maryland Public Service Commission: Holding company acquisition of utility holding company (2014-15).

Mississippi Public Service Commission: Utility holding company's divestiture of its utility subsidiaries' transmission assets to an independent transmission company (2013).

U.S. District Court for Minnesota: Effects of Minnesota statute limiting reliance on fossil fuels (2013).

Tobacco Arbitration Panel: Principles for regulating cigarette manufacturers (on behalf of State of Maryland) (2012).

Illinois Commerce Commission: Performance-based ratemaking (2012).

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"The Legal Standard of 'Prudent Utility Practices' in the Context of Joint Construction Projects," *NRECA/APPA Newsletter Legal Reporting Service* (Dec. 1984/Jan. 1985) (co-author).

## Speaker and Lecturer

**United States:** American Antitrust Institute; American Association of Retired Persons; American Bar Association; American Power Conference; American Public Power Association;

American Wind Energy Association; Chicago Bar Association (Energy Section); Columbia University Institute for Tele-Information; Electric Cooperatives of South Carolina; Electric Power Research Institute; *Electric Utility Week;* Electricity Consumers Resource Council; *Energy Daily;* Executive Enterprises; Exnet; Federal Energy Bar Association; Federal Energy Bar Association; Harvard Electricity Policy Group; Infocast; Louisiana Energy Bar; Management Exchange; Maryland Resiliency Through Microgrids Task Force; MIT Energy Initiative; Mid-America Association of Regulatory Commissioners; MidAtlantic Demand Resources Initiative; Mid-Atlantic Conference of Regulatory Utility Commissioners; National Association of Regulatory Utility Commissioners; National Association of State Utility Consumer Advocates; National Conference of Regulatory Attorneys; National Governors Association; National Independent Energy Producers; New England Conference of Public Utility Commissioners; New England Public Power Association; New York Bar Association (Energy Section); North Carolina Electric Membership Corporation; Pennsylvania Bar Institute; Puerto Rico Energy Policies Forum; Regulatory Studies programs at Michigan State University, New Mexico State University and University of Idaho; Society of American Military Engineers; Society of Utility and Regulatory Financial Analysts; Southeastern Association of Regulatory Utility Commissioners; U.S. Department of Energy Forum on Electricity Issues; U.S. Environmental Protection Agency; World Regulatory Forum; Yale Alumni in Energy.

**International:** Canadian Association of Members of Utility Tribunals; Canadian Energy Law Forum; Central Electric Regulatory Commission (India); Comisión Reguladora de Energía (Mexico); Independent Power Producers Association of India; India Institute of Technology at Kanpur; Ludwig-Maximilians-Universitat (Munich, Germany); Management Development Institute at Gurgaon, India; National Association of Water Utility Regulators (Italy); New Zealand Electricity Authority; New Zealand Commerce Commission; Nigeria Electric Regulatory Commission; Office of Utility Regulation of Jamaica; OSIPTEL (the Peruvian Telecom Regulator) Training Program on Regulation for University Students; Petroleum and Natural Gas Regulatory Board (India); Regulatel (an international forum of telecommunications regulators); Regulatory Policy Institute (Cambridge, England); The Energy and Resources Institute (India).

## Community Activities

Member, PEPCO Work Group, appointed by County Executive of Montgomery County, Maryland (2010–2011).

Sunday School Teacher, Temple Emanuel, Kensington, Maryland (2002–2006, 2008).

Board of Trustees, Temple Emanuel (2005–2006).

Musical performer (cello), Riderwood Village Retirement Community (2003–present).