

**BEFORE THE WASHINGTON STATE
UTILITIES AND TRANSPORTATION COMMISSION**

In the Matter of the Joint Application of)	DOCKET UG-061721
)	
MDU RESOURCES GROUP, INC.)	
AND CASCADE NATURAL GAS)	ORDER 06
CORPORATION)	
)	
For an Order Authorizing Proposed)	APPROVING AND ADOPTING
Transaction)	STIPULATION; AUTHORIZING
)	TRANSACTION
.....)	

Synopsis: The Washington Utilities and Transportation Commission approves and adopts an unopposed Stipulation that proposes by its terms to resolve all issues in this proceeding. The Stipulation includes 36 commitments from the applicants, including ring-fencing provisions to maintain Cascade Natural Gas Corporation’s financial independence from its new parent corporation and other corporate affiliates. The commitments preserve the Commission’s access to information necessary to its regulatory responsibilities, protect service quality, protect consumers from rate impacts and preserve low-income programs. Taken together, the commitments address the Commission’s concerns in connection with MDU Resources Group, Inc’s proposed acquisition of Cascade Natural Gas Corporation. The Commission, by this Order, authorizes the proposed transaction.

SUMMARY

1 **PROCEEDINGS:** Cascade Natural Gas Corporation (Cascade) and MDU Resources Group, Inc. (MDU Resources) filed a joint application on November 13, 2006, for an order authorizing MDU Resources’ acquisition of all outstanding common stock of Cascade. The Washington Utilities and Transportation Commission (Commission) convened a prehearing conference Olympia, Washington on December 6, 2006, before Administrative Law Judge Dennis J. Moss. The Commission, among other things, adopted an agreed schedule upon which to consider the joint application.

2 MDU Resources, Cascade, the Commission's regulatory staff (Commission Staff or Staff), the Public Counsel Section of the Washington Office of the Attorney General (Public Counsel), Northwest Industrial Gas Users (NWIGU), the Energy Project, and Boise Cascade LLC (Boise Cascade) filed a Stipulation on May 9, 2007, and requested that the Commission approve and adopt its terms in full resolution of the issues in this proceeding.¹

3 **PARTY REPRESENTATIVES:** James M. Van Nostrand and Laurence Reichman, Perkins Coie LLP, Portland, Oregon, represent MDU Resources and Cascade. Melinda J. Davison, Matthew Perkins and Sarah Yasutake, Portland, Oregon, represent Weyerhaeuser, Boise Cascade and Longview Fibre. John A. Cameron, Davis Wright Tremaine LLP, Portland, Oregon, represents Cost Management Services, Inc. Edward A. Finklea, Chad M. Stokes and Lindsay R. Kandra, Cable Huston Benedict Haagensen & Lloyd LLP, Portland, Oregon, represent NWIGU. Ron Roseman, attorney, Seattle, Washington, represents the Energy Project. Simon ffitich, Assistant Attorney General, Seattle, Washington, represents Public Counsel. Gregory Trautman, Assistant Attorney General, Olympia, Washington, represents Commission Staff.²

4 **COMMISSION DETERMINATIONS:** The Commission finds its adoption and approval of the parties' Stipulation will establish conditions that ensure the proposed transaction is consistent with the public interest. The Commission concludes it should approve the Revised Application filed by MDU Resources and Cascade on March 23, 2007, and authorize MDU Resources' acquisition of Cascade pursuant to the terms of the Revised Application, subject to the requirements included in the Stipulation.

¹ The remaining parties to this proceeding, Cost Management Services, Inc., Weyerhaeuser Company and Longview Fibre, are not signatories to, but do not oppose the Stipulation.

² In formal proceedings, such as this case, the Commission's regulatory staff functions as an independent party with the same rights, privileges, and responsibilities as any other party to the proceeding. There is an "ex parte wall" separating the Commissioners, the presiding Administrative Law Judge, and the Commissioners' policy and accounting advisors from all parties, including Staff. RCW 34.05.455.

MEMORANDUM

I. Background and Procedural History

- 5 MDU Resources and Cascade (Applicants) initiated Docket UG-061721 by filing on November 13, 2006, their joint application for an order authorizing MDU Resources' acquisition of all outstanding common stock of Cascade. The parties held a technical workshop on February 20, 2007, followed by a settlement conference on March 5, 2007. On March 23, 2007, Applicants submitted a Revised Application to incorporate modifications to the structure of the transaction, as agreed during settlement discussions. The parties held additional settlement conferences and reached agreement on the principal terms of a full settlement on April 20, 2007.
- 6 On May 9, 2007, MDU Resources, Cascade, Staff, Public Counsel, NWIGU, the Energy Project, and Boise Cascade, filed their Stipulation. They request that the Commission approve and adopt the Stipulation as a full resolution of all issues pending in this proceeding. By a letter filed on May 21, 2007, Weyerhaeuser stated that it does not intend to sign the Stipulation or become a party to it, but does not oppose its adoption. The remaining intervenors, CMS and Longview Fibre, stated no opposition to the Commission's adoption of the Stipulation.
- 7 The parties filed their narrative in support of the Stipulation on May 11, 2007. The narrative describes the proposed transaction in detail. According to the parties, the transaction will be completed in substantially the following manner:
- a. The transaction will be effected pursuant to a reverse triangular merger whereby MDU Resources will acquire all of the outstanding common stock of Cascade for a purchase price of \$26.50 per common share or approximately \$305 million in cash through Merger Sub, a subsidiary of MDU Resources formed specifically to effectuate the acquisition. At the effective time of the merger, Merger Sub will cease to exist.
 - b. The corporate organizational structure that MDU Resources anticipates after closing of the acquisition is set forth in the Post Acquisition Cascade Organizational Chart included as Attachment 1

to the transaction commitments.³ Without regard to the possible use of short term bridge financing (which if used would be repaid at the time permanent financing is put into place), the following steps describe the sequence of events MDU Resources anticipates in establishing Cascade as "ring fenced" in the support of a Non-Consolidation Opinion which Cascade commits to obtain under one of the commitments.

(i) MDU Resources will either issue new common equity or utilize other available capital resources to fund approximately \$220 million for the purchase of the existing Cascade stock.

(ii) Debtco, as identified in Attachment 1 and the Stipulation, will obtain approximately \$85 million of additional funds through debt financing to complete the funding for the purchase of the Cascade stock. Approximately \$165 million of existing debt at Cascade will remain at Cascade and be unaffected by the merger.

(iii) Approximately \$305 million will be transferred to a paying agent who will pay Cascade's existing shareholders. MDU Resources will make capital contributions to Debtco. Debtco will make capital contributions to Equico, as identified in Attachment 1 to Appendix A of the Stipulation, such that, upon the completion of the transaction, Equico will then own 100% of the stock of Cascade and Debtco will own 100% of the stock of Equico.

(iv) Equico's stock will be the asset supporting Debtco's loan of approximately \$85 million. Equico is expected to be established as a bankruptcy-remote special purpose entity, and is not expected to have debt.

(v) At least one director of Equico will be an Independent Director, as described in one of the commitments.

- c. In summary, MDU Resources plans to cause all of the common stock of Cascade to be owned by Equico, a new Delaware limited liability company and wholly-owned subsidiary of Debtco, also a Delaware limited liability company whose stock will be owned by MDU

³ The transaction commitments are included as Appendix A to the Stipulation filed with the Commission on May 9, 2007.

Resources. This structure and transactional flow result in the assets, liabilities and equity of Cascade remaining as presently recorded.

8 The Commission conducted a hearing to consider the Stipulation on June 18, 2007. Counsel for MDU Resources and Cascade, and Bruce T. Imsdahl, President and CEO of Montana-Dakota Utilities Co. (Montana-Dakota), a division of MDU Resources, made opening statements. The parties made available to the Commission for questioning a panel of witnesses including Dave Goodin, who will be Cascade's new president once the transaction is completed; John F. Renner, Executive Vice President, Finance and Chief Accounting Officer for Montana-Dakota; Jon T. Stoltz, Senior Vice President, Cascade Natural Gas; Ken Elgin for Commission Staff; Steven Johnson and Glenn Watkins for Public Counsel; and Paula Pyron for NWIGU.

II. Settlement Agreement

9 The parties recommend under the terms of the Stipulation that the Commission issue an order approving the transaction, imposing as conditions the 36 commitments set forth in Appendix A to the Stipulation. The Stipulation, including Appendix A, is attached to and made a part of this Order by this reference. Applicants' commitments include proposed conditions in the following areas:

- Access to relevant information.
- Rate credits and other rate issues.
- Cascade's financial stability.
- Ring-fencing provisions.
- Cost allocation and cross-subsidization issues.
- Low-income programs.
- Quality of service measures.
- Commitment implementation issues.

10 The settling parties, arguing that the Commission should find the Stipulation to be in the public interest, focus their joint testimony on the significant financial protections, particularly the ring-fencing provisions; the financial incentive of a \$672,000 per year rate credit commitment for five years; and insulation of customers from transactional

costs and increased operating costs attributable to the merger. Public Counsel adds service quality reporting commitments to its focus and the Energy Project emphasizes the several commitments to continue low income assistance and weatherization programs.

- 11 The settlement includes a “most favored state” clause to ensure Washington could receive the benefit of any additional commitments the companies make in Oregon where regulatory approval is also required.⁴

III. Discussion and Decisions

- 12 The standard under Chapter 80.12 RCW and WAC 480-143-170 for approval of transactions such as the one proposed here is that the Commission will deny an application if it determines "the proposed transaction is not consistent with the public interest."⁵ The Commission described this as a “no harm” standard in its Third Supplemental Order in Docket UE-981627, the 1999 proceeding in which the Commission approved the merger between PacifiCorp and ScottishPower PLC (ScottishPower case).

- 13 As we observed in the ScottishPower case, two threshold criteria in considering whether a merger of this type meets the no harm test are the acquiring company’s financial and managerial fitness to take over the acquired utility’s operations, including its ability to run those operations safely and reliably. Mr. Renner, responding to questions from the Bench, stated that MDU Resources, while acquiring Cascade, is simultaneously involved in other transactions that will result in a cash infusion sufficient to fund the acquisition in a manner that will be perceived by analysts as financially neutral. Thus, from the perspective of the financial markets, the transaction should cause no change in the corporate family’s financial condition. MDU Resources’ prefiled testimony includes significant evidence of the company’s financial fitness and also establishes its managerial fitness to run Cascade’s operations safely and reliably.⁶

⁴ The Public Utility Commission of Oregon approved a stipulation similar in its terms to the Stipulation pending before us and authorized the transaction on June 5, 2007, in Order 07-221.

⁵ WAC 480-143-170.

⁶ Exhibit 5 (Imsdahl Direct) at 5:4 – 8:7, 9:10 – 20:19 (managerial fitness); Exhibit 7 (Renner Direct) at 5:6 – 9:3 (financial fitness); 9:4 – 11:33, 13:8 – 16, 17:16 – 19:22 (managerial fitness).

- 14 The 36 commitments that are part of the Stipulation ensure that the Commission will have access to information necessary to continue to regulate Cascade. Cascade's financial statements and other financial books and records will be maintained separately from the books and records of MDU Resources. Furthermore, Cascade will maintain its own credit rating for the purpose of issuing debt and preferred equity separate from MDU Resources and its affiliates. Commitment 3 addresses the access to be provided to books of account, as well as all documents, data, and records of their affiliated interests, which pertain to transactions between Cascade and its affiliated interests or which are otherwise reasonably calculated to lead to discoverable information regarding Cascade. The Stipulation confirms that, as provided under Washington law or regulation, the Commission may audit the accounting records of MDU Resources and its subsidiaries or divisions that are the basis for charges to Cascade. Applicants agree to notify the Commission in the event of certain acquisitions by MDU Resources. The Commission will be kept apprised of written information provided by and to credit rating agencies pertaining to Cascade. Commitment 26 provides for access to corporate minutes that provide relevant information regarding Cascade's business and associated risk analysis. Cascade and MDU Resources agree to provide a copy of any report resulting from an audit or review undertaken by any regulatory body pertaining to cost allocations and affiliated transactions involving Cascade and MDU Resources' regulated operations.
- 15 The commitments provide for the measuring and reporting of certain service quality information to monitor the quality of service provided by Cascade after the transaction. To ensure service quality, the Stipulation includes measuring and reporting requirements in Commitment 22 for calendar years 2008 and 2009. These reports will be provided to the Commission, the parties to this docket and made available to the public within 90 days following the end of the calendar year. The reports will include significant detail concerning customer complaints and Cascade's responsiveness to customers in the ordinary course of business. This oversight program will be reviewed after December 31, 2009, and the Commission will receive a report recommending whether to continue the program in its proposed, or another, form.

- 16 The commitments address cost allocation and cross-subsidization issues to ensure that Cascade's Washington customers will bear only those costs associated with providing retail gas distribution services in Washington. Cascade commits to exclude all costs of the transaction, including acquisition premium and integration costs, from ratemaking. Further, if there are costs that Cascade incurs for improved efficiencies which are proposed for rate case consideration, Cascade commits to provide to the Commission's satisfaction a demonstration of a net benefit to customers. These commitments, in conjunction with other commitments that cap allocated costs and provide direct credits to customers, provide adequate assurance that there is no financial harm to customers from the transaction.
- 17 The commitments contain extensive ring-fencing provisions that will protect Cascade's customers from any adverse impacts associated with Cascade's ownership by MDU Resources, and include other financial protections such as limitations on Cascade's ability to declare dividends.⁷ The ring-fencing provisions will protect ratepayers from future financial risk, including the risk of MDU Resources' bankruptcy, upon which subject Cascade expressly commits to obtain a non-consolidation opinion within three months of closing the transaction. Other provisions protect ratepayers from the effects of affiliated interest transactions, require MDU Resources and Cascade to keep separate books, records, and assets, and require that MDU Resources and Cascade provide the Commission and Staff with access to these financial records so the Commission can continue to regulate effectively.
- 18 Apart from protecting against any adverse impacts associated with the transaction, the commitments also provide tangible, quantifiable benefits to Washington customers in the form of rate credits. Under Commitment 11, Cascade will provide \$672,000 in annual rate credits that cannot be offset for three years, and which thereafter may be offset in a general rate case only under certain conditions.
- 19 Having just initiated two new programs with Cascade – the energy efficiency program begun in the fall of 2005 and the energy assistance program established as an outcome

⁷ In addition to dividend restrictions, Applicants agree in Commitment 29 to provide notice to the Commission when Cascade's dividend payment increases by 10% or more relative to dividends for the previous quarter.

of the Company's most recent rate case – and being unfamiliar with the practices and policies of Montana-Dakota Utilities, the Energy Project stated its concerns about the future of the low-income assistance programs. Commitments 33, 34, and 35 address these concerns by ensuring that Cascade will continue to work cooperatively with the Energy Project and the relevant community-based organizations delivering these programs to provide bill assistance, and improve the delivery of energy efficiency measures to gas-heated low-income homes.

20 In summary, the commitments undertaken here by MDU Resources and Cascade address comprehensively the range of concerns expressed by the parties to this proceeding, and the Commission's concerns as indicated in previous cases involving transactions of this type. We are satisfied on the basis of our review of the record that the proposed transaction, conditioned by the terms of the Stipulation, is consistent with the public interest, thus meeting the applicable statutory and regulatory standards for authorization pursuant to chapter 80.12 RCW and WAC 480-143-170.

FINDINGS OF FACT

21 Having discussed above in detail the evidence received in this proceeding concerning all material matters, and having stated findings and conclusions upon issues in dispute among the parties and the reasons therefore, the Commission now makes and enters the following summary of those facts, incorporating by reference pertinent portions of the preceding detailed findings:

22 (1) The Washington Utilities and Transportation Commission is an agency of the State of Washington, vested by statute with authority to regulate rates, rules, regulations, practices, and accounts of public service companies, including gas companies.

23 (2) Cascade is a "public service company" and a "gas company" as those terms are defined in RCW 80.04.010 and used in Title 80 RCW. Cascade is engaged in Washington State in the business of supplying utility services and commodities to the public for compensation.

- 24 (3) MDU Resources' acquisition of Cascade on the terms provided by their Revised Application, as conditioned by the terms of the Stipulation attached to and made a part of this Order by prior reference, including the 36 commitments set forth in Appendix A to the Stipulation, is consistent with the public interest.

CONCLUSIONS OF LAW

25 Having discussed above all matters material to this decision, and having stated detailed findings, conclusions, and the reasons therefore, the Commission now makes the following summary conclusions of law, incorporating by reference pertinent portions of the preceding detailed conclusions:

- 26 (1) The Washington Utilities and Transportation Commission has jurisdiction over the subject matter of, and parties to, these proceedings.
- 27 (2) MDU Resources' proposed acquisition of Cascade on the terms provided by their Revised Application, as conditioned by the terms of the Stipulation attached to and made a part of this Order by prior reference, including the 36 commitments set forth in Appendix A to the Stipulation, meets the standards for approval as set forth in Chapter 80.12 RCW and WAC 480-143-170. The Commission should authorize the proposed transaction.

ORDER

THE COMMISSION ORDERS:

- 28 (1) The parties' Stipulation, filed in this Docket on May 9, 2007, is approved and adopted in full resolution of the issues pending in this proceeding.
- 29 (2) MDU Resources' acquisition of Cascade on the terms provided by their Revised Application, as conditioned by the terms of the Stipulation attached to and made a part of this Order by prior reference, including the 36 commitments set forth in Appendix A to the Stipulation, is authorized.

- 30 (3) Cascade is authorized and required to make any compliance filing necessary to effectuate the terms of this Order.
- 31 (4) The Commission Secretary is authorized to accept by letter, with copies to all parties to this proceeding, a filing that complies with the requirements of this Order.
- 32 (5) The Commission retains jurisdiction to effectuate the terms of this Order.

Dated at Olympia, Washington, and effective June 27, 2007.

WASHINGTON STATE UTILITIES AND TRANSPORTATION COMMISSION

MARK H. SIDRAN, Chairman

PATRICK J. OSHIE, Commissioner

PHILIP B. JONES, Commissioner

NOTICE TO PARTIES: This is a Commission Final Order. In addition to judicial review, administrative relief may be available through a petition for reconsideration, filed within 10 days of the service of this order pursuant to RCW 34.05.470 and WAC 480-07-850, or a petition for rehearing pursuant to RCW 80.04.200 and WAC 480-07-870.

STIPULATION