

September 26, 2016

**VIA EMAIL: [townmanager1@new-shoreham.com](mailto:townmanager1@new-shoreham.com)  
AND REGULAR FIRST CLASS MAIL**

Ms. Nancy Dodge  
Town Manager  
Town of New Shoreham  
P.O. Box 220  
Block Island, RI 02807

Re: BIPCo Environmental Costs

Dear Ms. Dodge:

Our firm has been engaged to, among other things, oversee and provide legal advice on the environmental due diligence conducted as part of the Town of New Shoreham's planned acquisition of two-thirds of the issued and outstanding stock of Block Island Power Company ("BIPCo"). As part of that diligence, SAGE Environmental, Inc. ("SAGE") conducted an ASTM Phase I environmental site assessment, as amended by addendum, and a comprehensive groundwater sampling program at the BIPCo property, located at New Shoreham Tax Assessor Plat 17, Lots 35, 36, 37, and 40 (the "Property"). See SAGE Phase I Environmental Site Assessment dated September 15, 2016 (including Executive Summary) and SAGE Phase I Environmental Site Assessment Addendum dated September 20, 2016 (collectively, the "Phase I Report"); and SAGE Groundwater Summary Sampling Report dated September 22, 2016 (the "Groundwater Report"). That assessment identified several environmental conditions at the Property that are currently being addressed or will need to be addressed. You have asked whether future costs associated with attending to those identified conditions are of the type that can be properly charged to BIPCo's ratepayers as part of BIPCo's operational expenses and as part of future rate making. As explained more fully below, we believe that the environmental costs that BIPCo will or may incur after the stock purchase are fairly characterized as compliance costs required as part of State-approved cleanup activities and by applicable environmental regulation. As such, we believe that such costs would be reasonable and appropriate to pass onto the ratepayers.

One of the environmental conditions at the Property is residual petroleum contamination associated with the past removal of numerous underground storage tanks associated with a former filling station in the northern portion of the Property, and with a historical tank farm in the southern portion of the Property. To address the contamination, active groundwater remediation systems were put in place and were active from the early 1990s to 2006 pursuant to cleanup plans approved by the Rhode Island Department of Environmental Management (the "Department"). In 2006, the Department approved termination of those systems in favor of monitored natural attenuation ("MNA"). MNA consists of periodic monitoring and reporting of groundwater contaminants until their concentrations decrease to or below regulatory standards. MNA is a long-term remedial strategy; accordingly, reaching contaminant concentration objectives can take years, even decades. The Phase I Report indicates that such monitoring has occurred and that the data going back to 2006 shows an overall decrease of contaminant concentrations with the exception of benzene in the northern portion of the property (which has had fluctuating concentrations over the years). The groundwater sampling results collected by SAGE in September, 2016 confirm the presence of those groundwater contaminants in the same range of concentrations as that reported to the Department previously.

In order to address known residual petroleum contamination at the Property, groundwater monitoring and reporting will continue "until monitored natural attenuation (MNA) reduces residual petroleum impacts to compliant levels." See SAGE Groundwater Report, at 1.

Other environmental conditions relate to the above-ground storage and use of petroleum products or waste oil at the Property, as well as the storage of No. 2 heating fuel and diesel fuel in five remaining, 20,000-gallon underground storage tanks ("USTs"). Several of the diesel fuel USTs are used for the company's backup generators. Based upon the SAGE groundwater data, it does not appear that BIPCo's current use and storage of oil and waste oil at the Property is causing or contributing to releases at the Property. In addition, the five USTs are reported to have passed tank tightness tests in May, 2016. See SAGE Phase I Report, at 14.

While there is no indication that these other environmental conditions have resulted in releases at the Property, SAGE does recommend that storage practices be changed in order to mitigate the risk of a future release and that a soil management plan be prepared and implemented as part of any future land disturbing activities. SAGE also notes that the five USTs must be removed and closed out with the Department. Due to their age and construction, the USTs must be removed by December 22, 2017, pursuant to applicable state regulation. See Rules and Regulations for Underground Storage Facilities Used for Petroleum Products and Hazardous Materials (2011), at Rule 8.04(A). SAGE has estimated the cost to remove and close out those USTs to be in the range of approximately \$210,000 to \$260,000, with the installation of replacement above-ground storage tanks to be in the range of approximately \$200,000 to \$250,000. See attached SAGE proposal for UST removal and replacement dated September 23, 2016 (excluding soil and groundwater waste disposal costs if applicable).

The above-described actions that are required to be undertaken or are recommended to be undertaken at the Property are for the purpose of ongoing environmental compliance at the Property. In particular, the Department requires continued monitoring and reporting as part of previously-approved cleanup plans and the UST removal must be done to comply with applicable regulation. Historically, the costs to run the remedial systems at the Property and conduct ongoing monitoring of groundwater have been passed onto to BIPCo's customers. In 1991, the Rhode Island Public Utilities Commission ("PUC") approved an "environmental remediation surcharge" of \$0.00895 per kilowatt-hour that was added to customer electric bills through 2000. See PUC Order 13769. In 2000, that surcharge was renewed for an additional year but lowered to \$0.00729 per kilowatt-hour. At that time, the PUC noted that environmental remediation "was necessary" and that the surcharge was "reasonable and in the best interests of the ratepayers." See PUC Order 16365 dated August 28, 2000, attached hereto. Further, as part of the last rate hearing in 2005, we are informed that that the PUC allowed as part of the approved rate for rate year 2005-06, operational expenses that included \$42,817 in environmental compliance costs such as environmental engineering, treatment system operations and maintenance, tank registration fees, air operating permit fees, and emissions tests. Environmental compliance expenses reported for fiscal years 2001-2005 were \$60,000, \$62,000, \$44,000, \$31,000, and \$70,000 respectively. Because these costs were incurred during the time that active remedial systems were operational, it is assumed that current compliance costs – consisting of quarterly monitoring and reporting – are appreciably lower.

It is reasonable to assume that the PUC would approve as part of future rate making ongoing environmental compliance costs arising from the same environmental conditions that gave rise to previously approved costs. Indeed, costs to ensure ongoing compliance with Department directives under approved cleanup plans would be a "reasonable and just" operating cost to recover from ratepayers. See R.I. Gen. Laws § 39-2-1 (utility rates and charges must be "reasonable and just"). Further, passing on the costs of the removal of the five tanks by the end of 2017, per mandatory Department regulation, is also reasonable and necessary in order to have a compliant Property. Indeed, most of the remaining tanks are used, and any future replacement tanks would be used, for the direct purpose of providing electric service. Accordingly, it is expected that BIPCo would be able to demonstrate the necessity of these costs in order to continue to use and operate the Property, as well as to provide appropriate service to BIPCo's customers. See R.I. Gen. Laws § 39-3-12 (company bears the burden of proof to show that its rate increase is necessary in order to obtain just and reasonable compensation for the service rendered).

The anticipated approval of these mandatory compliance costs by the PUC would be consistent with not only its past approvals but by what other state commissions have allowed in rate cases by utilities seeking to recover similar costs. See, e.g., Attorney General v. Michigan Public Service Commission, 463 Mich. 912 (2000) (environmental remediation costs were just and reasonable because they were incurred pursuant to mandatory environmental law, were necessary to operate, and were based upon utility's ownership of current property); Matter of

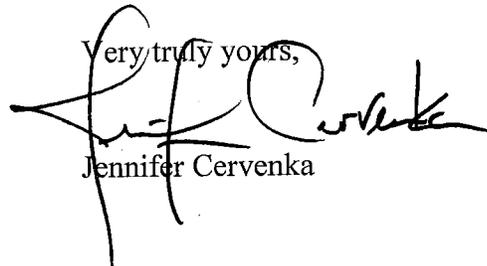
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Request of Interstate Power Co. for Authority to Change Its Rates for Gas Service In Minnesota, 574 N.W.2d 408 (MN 1998) (fair and reasonable to have ratepayers contribute to environmental cleanup costs of utility despite costs incurred for historic activities for slightly different service); Citizens Utility Board v. Illinois Commerce Commission, 166 Ill.2d 111 (1995) (environmental remediation costs prudently and reasonably incurred because they are part of current costs of doing business, legally mandated, and conferred benefit on utility customers).

While case law indicates particular circumstances where environmental costs would not be appropriate to pass onto ratepayers, we are not aware of any such circumstances being present here. For example, some jurisdictions have denied environmental costs where the costs have no nexus to the service rendered by the utility, or where the expenses have been the result of waste, inefficiency, or bad faith. BIPCo's monitoring costs arise from the ownership and maintenance of the same property from which it has and will continue to provide electric service to its customers. Moreover, most of the remaining USTs that must be removed and replaced store diesel fuel which is used for the company's backup generators. Accordingly, those costs are for the most part directly related to the provision of services to BIPCo's customers. Lastly, there is no evidence of bad faith or waste where BIPCo has performed its remedial activities under State approved cleanup plans for the better part of the last twenty-five years, and the Property is currently in a stable, monitored condition.

Based upon the above, it is our opinion that the environmental compliance costs that will be incurred by BIPCo following the Town's purchase of two-thirds of the outstanding shares will be properly characterized as reasonable and just operating expenses of BIPCo recoverable from its ratepayers.

Very truly yours,



Jennifer Cervenka

JRC:jwb  
Enclosures (2)  
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