STATE OF NEW HAMPSHIRE

PUBLIC UTILITIES COMMISSION

July 25, 2017 - 10:00 a.m.
Concord, New Hampshire

RE: DW 16-806
PENNICHUCK WATER WORKS, INC.
Request for Change in Rates

PRESENT: Commissioner Martin P. Honigberg,Presiding
Commissioner Kathryn M. Bailey

Sandy Deno, Clerk

APPEARANCES: **Reptg. PENNICHUCK WATER WORKS, INC.:**
Richard W. Head, Esq. (Rath,Young...)

Reptg. RESIDENTIAL RATEPAYERS
D. Maurice Kreis, Esq. (Cons. Adv.)
James Brennan, Finance Director

Reptg. PUC STAFF:
John Clifford, Esq.
Mark Naylor, Dir./Gas & Water Div.
Jayson Laflamme, Gas & Water Div.
Robyn Descoteau, Gas & Water Div.

COURT REPORTER: SUSAN J. ROBIDAS, NH LCR NO. 44

I N D E X

P R O C E E D I N G S

CHAIRMAN HONIGBERG: Good morning, everyone. We're here in Docket 16-806, which is the Pennichuck Water Works rate case. We're here for a hearing on the merits, and we have a Settlement Agreement that's been filed.

Before we do anything else, let's take appearances.

MR. HEAD: Richard Head with Rath, Young, Pignatelli, on behalf of Pennichuck Water Works. Seated with me at counsel table is Larry Goodhue, also with Pennichuck, and Donald Ware. And then behind me are Jake Kerrigan and Carol Ann Howe.

MR. KREIS: Good morning, Mr. Chairman, Commissioner Bailey. I'm D. Maurice Kreis, the Consumer Advocate here on behalf of residential utility customers. And seated to my left is our Director of Finance, James Brennan.

MR. CLIFFORD: Good morning, Commissioners. John Clifford, on behalf of Commission Staff. And seated next to me at counsel table is Mark Naylor, Director of the Gas and Water Division, as well as Jayson

Laflamme, Staff analyst of the Gas and Water Division, and Robyn Descoteau.

CHAIRMAN HONIGBERG: All right. Before we get started, are there any preliminary matters we need to deal with, Mr. Clifford?

MR. CLIFFORD: There are just very slight preliminary matters, in that we've taken some illegible pages in the Settlement and we've replaced those and given you more legible copies of those. They are complete copies of what you've seen in the filing.

And then we would like to make, actually, one correction to the Settlement Agreement. We spotted one error. If you'll turn to Bates Page 8, Page 7 of the Settlement Agreement, Section B, parties are agreeing to a permanent rate increase of $887,591, or 3.12 percent, effective on a bills-rendered basis. And here's where the change comes in. It should be "on or after December 7, 2016," not "2017." And that is the only ministerial correction that we have today. And we apologize for that error, but it just didn't get picked up.

CHAIRMAN HONIGBERG: All right. Other than that, how are we proceeding this morning?

MR. CLIFFORD: Our plan was to put up Mr. Mark Naylor on behalf of Commission Staff, and he will start the proceeding. Then I will intend to hand it over to Attorney Head, who will speak to his panel of witnesses, which I believe is just going to be Mr. Goodhue. And the OCA will also offer up its staff analyst, and they will have questions.

CHAIRMAN HONIGBERG: Are the witnesses going to testify as a panel, or are they doing it individually?

MR. CLIFFORD: They will -- we will put them up as a panel.

CHAIRMAN HONIGBERG: All right. Why don't we have them take their places.

MR. CLIFFORD: And Mr. Laflamme, too. Sorry to interrupt. Mr. Laflamme will be up there, too.

CHAIRMAN HONIGBERG: So there will be four witness up there.

Other than that, any there any

other preliminary matters we need to deal with for anybody?

MR. HEAD: No.

CHAIRMAN HONIGBERG: All right.

MR. HEAD: Mr. Chairman, there is one document we referred to a lot that's part of the Settlement package. If I could hand that to you just so you don't need to keep flipping back and forth, would that be useful?

CHAIRMAN HONIGBERG: Sure.

(WHEREUPON, LARRY D. GOODHUE, MARK NAYLOR, JAYSON LAFLAMME AND JAMES BRENNAN were duly sworn and cautioned by the Court Reporter.)

CHAIRMAN HONIGBERG: Mr. Clifford.

DIRECT EXAMINATION

BY MR. CLIFFORD:

Q. Mr. Naylor, I'd like you to briefly state your full name and position with the Commission, and I'd like to ask you a couple questions.

A. (Naylor) Yes. My name is Mark Naylor. I'm the Director of the Gas and Water Division here at the New Hampshire Public Utilities Commission.

Q. And Mr. Naylor, are you fully -- are you familiar with the Settlement Agreement that's been filed in this case and the negotiations leading up to this Settlement Agreement?

A. (Naylor) Yes.

Q. And in your opinion -- or do you have an opinion as to what the Commission should do with this Settlement Agreement?

A. (Naylor) Well, the Staff and Pennichuck Water Works and the Consumer Advocate's Office all agree that this is a good outcome for this docket. We are moving to a different, a little bit different ratemaking methodology than previously established in the Acquisition docket, which was 11-026. And we recommend it, and we will provide the details here this morning.

Q. Okay. Can you provide the Commission with just a high-level overview of this new ratemaking structure and the reasons why Staff is in support of this Agreement and the new structure going forward?

A. (Naylor) Yes. There are a hand -- a small handful of large points I would say to how we're proposing this Company and it's two sister utilities, Pennichuck East Utility and Pittsfield Aqueduct Company, to be regulated to have their rates set in the future. This Settlement Agreement calls for moving to a cash flow model for rate setting. It's similar to how municipal systems are regulated. But we believe we've done it in a way that avoids any CWIP issues, Construction Work In Progress, such that all assets must be complete and in service to customers before they are included in rates.

So, with a cash flow model, we have established a method of determining the revenue requirement, which is essentially the sum of three items. Similar to the originally established protocols in 11-026, one piece of that puzzle is each utility's share of the City's acquisition debt. It's called the "City Bond Fixed Revenue Requirement." That was established in the Acquisition docket. So the first number is that principle and interest that is PWW's share.

The second component is new in this Settlement Agreement, and we're calling it the "Operating Expense Revenue Requirement." And that's pretty much self-explanatory. That's further broken into two components. I'm not going to get into that right now. That's going to be detailed shortly after this. But there's a reason for having it in two components.

And then the third piece is the Debt Service Revenue Requirement. And this is really where we've really shifted the rate-setting process to a cash flow basis. We are substituting principle and interest payments for what traditionally has been return on rate base and depreciation expense. Why are we doing this? Primarily because this company and its two sister utilities have no equity. That was acknowledged in the Acquisition docket. That's how these companies were going to be capitalized going forward. And so with no equity, there's no concern about return to shareholders.

So I want to get to all the rest of the reasons in a moment, but I want to just complete my highlights of the ratemaking process as we propose it.

As I said, there is no more return on rate base and no more depreciation expense. Those are replaced by principle and interest on the Company's existing debt issues. We're also moving towards a different approach to the Rate Stabilization Fund that was established in the Acquisition docket. As part of that docket, $5 million of the city's acquisition debt was allocated to our Rate Stabilization Fund, and that was intended to essentially backstop the payment of the city's principle and interest payments on the acquisition of debt. That $5 million is now proposed to be broken into a few different pieces.

First of all, a share of it will be allocated to Pennichuck East Utility and a share will be allocated to Pittsfield Aqueduct Company. That will happen in future proceedings involving those companies. That allocation process will leave PWW Rate Stabilization Funds in an amount around $3.9 million. That 3.9 is now going to be allocated to backstop three components of the revenue requirement, and it's going to remain for the City Bond Fixed Revenue Requirement. A piece of it will backstop certain components of the Operating Expense Revenue Requirement. And the third component will backstop the Debt Service Revenue Requirement. So these new funds, which are the same money it was before, is just going to be allocated differently, with a slightly different purpose. And the objective there is to provide stability over time. With a company that's all debt and no equity, it's very important that the Company be able to access the debt markets at all times. And the use of these funds in this way should certainly help the Company access capital continuously, because the Company has, I believe about a $9 million per year, roughly, capital budget. So it's in that neighborhood. It's always going to need funds, just like all utilities.

And finally, the last of the highlights is the establishment of what we're affectionately calling the "QCPAC," Qualified Capital...

MR. CLIFFORD: Project Annual Adjustment Charge? Would that be the name of it?

A. (Naylor) Qualified Project Annual Adjustment Charge. Thank you. We've brought a lot of new acronyms in to water regulation with this Settlement. And this takes the place of the Company's current WICA, which is Water Infrastructure and Conservation Adjustment. And it is an annual filing, where the Company will bring in a filing with the details on its completed capital projects for the previous year and will seek the increase in revenues based on the completed capital projects, and it will not seek a return on those projects. It will seek principle and interest that's related to those projects. So those are the highlights of the new structure.

Now, why are we agreeing to this? At the Prehearing Conference in this proceeding last November, Staff, after preliminary review of the docket, had expressed concerns primarily about the proposal to add dollars to the revenue requirement for payment to the City of Nashua to reimburse the City for costs that it had incurred in an eminent domain proceeding some years ago. And we expressed concern that that potentially led to a slippery slope, where if that was permitted, then there may be other requests in the future for including in rates non-water service costs. The Company has agreed to drop that request. And in fact, we have put language, additional language in this Agreement which I think is very clear. And I do want to draw the Commission's attention to that just for a moment. It's Bates Page 24 of the Agreement, Paragraph E near the bottom of the page. This is, to me, perhaps one of the most important provisions of this document, and it's just coincidence that it's the last provision of the document.

But I want to draw your attention to the second full sentence that begins, "The Settling Parties agree and recommend that the Commission should clarify and require that neither PWW, PEU or PAC may collect revenues from customers for the purpose of distributing cash to Penn Corp." -- which is the parent of the three utilities -- "or ultimately as a special dividend or other form of distribution to the City to reimburse eminent domain costs or for any other purpose whatsoever."

And it goes on to say, "The Settling Parties further agree and recommend that the dividend restrictions contained in the DW 11-026 Settlement Agreement remain in full force and effect."

Staff's position has been, and Staff's position as reflected in this document is that it would not be appropriate to move this company or either of its two sister companies to a cash flow basis of rate setting if dividends could be declared and paid to the shareholders. The shareholder has no equity in this company. Furthermore, there are several thousand customers who live outside the city of Nashua, and it would be totally inappropriate for those customers to be paying through their rates for non-water service costs. So, with this in place, we were much more comfortable moving forward with restructuring this company's rate-setting process to what I just highlighted.

Some of the other considerations that Staff has taken into account, we certainly had to be convinced that this new approach would be of benefit to customers, and I believe it is. And I believe that Mr. Goodhue will provide you with testimony that will indicate that this company will be able to access capital at very reasonable rates. Its lenders and bankers will be assured that the Company will have the wherewithal to repay debt that it takes out. Its credit rating should be improved. And it's not bad now.

So, really what we're looking at is that Pennichuck Water Works is essentially a non-profit company. And certainly in this world now, with a company that's a hundred percent debt and zero percent equity, it's a crucial objective to keep borrowing rates as low as possible. There's some other things that we've built into this Agreement that I think are beneficial to customers. For example: The Rate Stabilization Funds that I briefly highlighted, if those become, I believe it's 150 percent of their set value, meaning that the Company has increased sales, there's a mechanism for those funds to be returned to customers. Conversely, if the Company has a couple of bad years and those funds are drawn down below their level at the next full rate proceeding, then customers will be asked to replenish them. But the whole idea with this is to keep the Company's cash flow stable, to ensure that it can borrow when it needs to and that it continues to be operated essentially as a non-profit. And that concludes my summary.

Q. Thank you, Mr. Naylor.

MR. CLIFFORD: I don't have any further questions of Mr. Naylor.

CHAIRMAN HONIGBERG: Mr. Head.

MR. HEAD: Thank you, Mr. Chairman.

DIRECT EXAMINATION

BY MR. HEAD:

Q. Mr. Goodhue, can you briefly describe your current position and former positions with the Company.

A. (Goodhue) Yes. My name is Larry Goodhue. I am the CEO of Pennichuck Corporation and its five subsidies. I assumed that role on November 6th of 2015. Prior to that, I hired on to the Company in 2006 as the comptroller of the Company. In April of 2012, after the Acquisition Order of 11-026, I was promoted to CFO of the corporation and its subsidiaries, and assumed the role of CEO as I indicated in 2015. I still also hold the title of CFO and treasurer for the corporation and its subsidiaries.

Q. And in terms of your current job duties, can

you just briefly describe what it is you do
in your position?
A. (Goodhue) Yeah. I'm responsible for the
overall financing, management and operation
of the corporation, along with our management
team. I report directly to the Board of
Directors of Pennichuck Corporation and to
the Board of Directors for each of the
subsidiaries. I also act as the liaison to
outside stakeholders and reporting agencies
on behalf of the Corporation, including the
bond rating agencies.
Q. And you're familiar with the Settlement
Agreement that's involved in this case?
A. (Goodhue) Yes, sir.
Q. You actively participated in meetings and its
development?
A. (Goodhue) For this case, yes.
Q. For this case. Before we get into details,
can you also just briefly remind the
Commission as to the structure of Pennichuck
Corporation and where Pennichuck Water Works
fits in?
A. (Goodhue) Yes, sir. Pennichuck Corporation

has one shareholder, the City of Nashua, as established under 11-026. Pennichuck Corporation is the parent to five subsidiary corporation, three of which are regulated utility corporations as Mr. Naylor has referred to, being Pennichuck Water Works, Incorporated, Pennichuck East Utility, Incorporated, Pittsfield Aqueduct Company, and then two non-regulated utilities subsidiaries, Pennichuck Water Service Corporation, as well as the Southwood Corporation. Pennichuck Water Service Company operates approximately 85 contracts for water systems, small to large, owned by others, and the Southwood Corporation is a land-holding subsidiary of Pennichuck Corporation.

Q. And how did the -- very briefly again, how did the City's acquisition affect the way in which Pennichuck Water Works operates as a utility?

A. (Goodhue) Under 11-026 there were some fundamental changes to the pre-existing rate methodology as an investor-owned utility, where we had both a debt and equity structure; we had a return on investment and return on equity. Under 11-026, the "CBFRR," as Mr. Naylor referred to it, the City Bond Fixed Revenue Requirement, was established as a fixed revenue component of the overall allowed revenue component. That was approximately about 27, 28 percent of the total revenue requirement as of that case which provided PWW's share of the monies that are needed to be provided up to Pennichuck Corporation for the servicing of the debt that was issued by the City in order to acquire Pennichuck Corporation. It also established the Rate Stabilization Fund, as Mr. Naylor indicated, of $5 million as a backstop to that fixed payment. The balance of the revenues were variable revenues based on consumption in the allowed revenue component.

Q. And how does that affect sort of the operations of Pennichuck Water Works, in terms of what the 11-026 system did and what we're proposing with this system?

A. (Goodhue) There's a couple of things that happened out of 11-026. Moving to a model where basically we don't have a return on equity in 11-026, there was also a fixed component for the return on equity being at or over a T-bill rate. And actually, the equity we can earn on is equity that is earned in a given tax year, because on an annual basis all the monies are flowed up to the parent corporation, dividended up in support of the CBFRR. So as a result, it created a cash flow problem, as Mr. Naylor had referred to, in that the methodology where the return on rate base and the depreciation expense did not give a one-to-one match of the debt, being a debt-funded-only entity. You needed to have depreciation lives and debt lives match up 100 percent in order for depreciation to get 100 percent coverage for principle repayment, which is not the case. Our depreciation lives far exceed our available terms of debt issuance.
Q. So how have you implemented the transition

from this equity-base to debt-base model?

A. (Goodhue) There's a couple things that have happened in the interim since the 2012 test year rate case, in that we've had two major rounds of financing that were completed in 2014 and in 2015. They were the first time that we were able to go to the debt market to actually raise the funds for the capital and infrastructure replaced with the Company. That gave us the ability to test what the markets would see, what the requirements would be, and how we were able to access those funds. So in those dockets we were able to fund capital for 2013, 2014, 2015 and 2016 in the 2014 financing, and in the 2017 financing, fund the construction of our new operations and distribution facility. At the same time, we also were able to refinance all of the legacy balloon maturity, tax-exempt bonds that had been floated by the corporation in two different opportunities in 2005 and one in 1996. Those were all balloon maturity bond offerings.

When the Company was an investor-owned

utility, the ability to go out with balloon maturity debt was a viable option because when that debt came to mature and we had to pay 100 percent of the balloon maturity, we had the option of either refinancing that debt with new debt, to the extent there was estimated useful life available and bondable appetite, or, more importantly, we could go to the equity markets and actually raise equity capital to repay that debt.

Under 11-026, that second option no longer became available. It was not available to us. And in testing this with the bond underwriters at the time of doing these financings, what we discovered was there was a problem relative to the actual ability to refinance that debt when it became due because there may not have been sufficient remaining useful life on the underlying, originally financed assets to actually re-bond that debt. So it created a problem that was on the horizon in addition to the cash flow problem that existed on an annual basis.

Q. So, just to summarize, what have you learned as to what has led to these modifications in the current Settlement Agreement based upon what you -- what's happened since 11-026?

A. (Goodhue) In those financing proceedings, those were an opportunity for us to go to the debt markets and say, What is really needed? How do we finance this corporation for long term? We do invest $8- to $10 million a year in capital for ongoing infrastructure replacement, so we need to have access to that debt. And what we were able to do was to test the underlying tenets of 11-026 with the bond markets. One of the positive things that came out of there, when they understood the fixed revenue component --

(Court Reporter interrupts.)

A. (Goodhue) I'm sorry. When they understood the fixed component of the CBFRR and the backstop of the Rate Stabilization Fund, they understood that there was not an equity payout to a shareholder. They were able to take that into consideration. It allowed us to not only refinance those pre-existing balloon maturity obligations, but to close those bond indentures which had covenants that were problematic and were actually going to be violated as early as last year, 2016. That also gave them the opportunity to look at our credit rating. Prior to the 11-026 order, we were the equivalent of a Triple B credit. We are now an A-plus Stable credit. So, with the 2014 order of financing, we went from Triple B to A, and since then have been upgraded to A-plus Stable. So, you know, that bears real benefit to our ratepayers, in that our cost of borrowing has gone down relative to an enhanced credit rating.

It also gave us a chance to peek behind the curtain as to what would be the requirements relative to enhancing that further and ensuring that we could repay our debt, because the debt that was done in '14 and '15, rather than being balloon maturity debt, was all financed as fully amortizing debt. They were serialized bond issuances modeled to as closely as possible create a fixed annual payout. So, with varying maturities and interest rates, on an aggregate, that was much lower than our pre-existing cost of debt and providing for an annual fixed cash payment that was roughly equal over the entire repayment time. So, based on that, that gave us a real good sense of what our cash flow needs would be if we could get a rate modification to actually tie to our ownership structure and our ability to raise debt to properly finance the Company.

Q. If you were able to give your lenders greater comfort in terms of the revenue stream and the RSF structure, what would that mean to the Company in terms of cost of borrowing? What are the three things that would affect?

A. (Goodhue) Well, No. 1, again, we've kind of error-checked this with our pre-existing bond underwriters. We haven't gone to the credit rating agencies yet, in that you can't put the chicken before the egg, as far as, you know, the cart before the horse, in that, you know, until we have a rate structure, we don't want to necessarily ask them to rate on that.

But we've checked this with both our bond underwriters, as well as our commercial lenders. The things that they see are the possibilities of lower interest rates, better access to the credit markets, and more favorable covenant requirements on bond debt -- on bonded debt perhaps in the future, or actually the ability to at least meet our existing bond covenants under a much more favorable method.

When we did those financings, we radically changed the covenants that were tied to our bond offerings and put bond covenants that were roughly equivalent to municipal bond-issuance covenants, which are basically cash flow-based.

Q. And Mr. Naylor briefly outlined the Settlement, and we'll go into a little more detail in just a minute.

But based on your experience, what do you believe the changes we're going to describe will provide to -- what benefits will that provide to PWW and its customers directly?

A. (Goodhue) I'm sorry, sir?
Q. In terms of the Settlement that we're about to go through in more detail, what are the specific benefits that this Settlement will provide to the customers of Pennichuck Water Works?
A. (Goodhue) Sure. There's a number of things that it will benefit our customers. No. 1, I believe that it is going to at least support the existing credit rating and/or enhance it, which will offer us access to debt at the lowest rates possible available for us. It will also offer up a methodology where you would have rateable increases over time. We talked about the QCPAC, or QCPAC methodology. Currently, we have WICA in place at the Company which allows for an annual surcharge, but only on a subset of our total capital investment; whereas, the QCPAC is all-encompassing relative to that investment. And so what happens is with that annual process, as we're investing the Company, it could be smaller rateable increases versus rate shock in a rate case, as far as that

spike. It's also going to give us the ability to provide EBITDA, Earnings Before Interest, Taxes, Depreciation and Amortization, at levels that would meet our covenant requirements not only on PWW's bonded debt, but also on the covenants that are in existence for the line of credit at Pennichuck Corporation, which is the working capital backstop for each of the subsidiaries on a daily basis. EBITDA is a very key financial measurement that the banks focus on. It's a measure of profitability, insuring that you're providing enough cash to pay your obligations. It will also provide the ability to adequately and continually meet the operating needs of the Company for its CBFRR payments, its debt service obligations and its operating expenses. It provides for a rate structure that is tied to cash flow and not to generate excess profits. It's also to provide for adequate cash flow in years where consumption patterns are below allowed levels, as well as in years where they're above allowed levels, in that you have the Rate Stabilization Funds to backstop that. And so it allows us to exist to pay for those various requirements without seeking rate relief at frequent intervals with our ratepayers.

Q. Can you speak briefly as to how this will affect the variability of revenue as an income stream?

A. (Goodhue) Yes. Under 11-026, roughly, approximately 28 percent of our revenue requirement became --

(Court Reporter interrupts.)

A. -- became 28 percent fixed and about 72 percent variable. Under this revised methodology, approximately 96 percent of our revenues are going to be fixed and about 4 percent variable.

So what does that mean? Under 11-026, if we had a very hot, dry summer like we did last year and we created excess revenues, only about 28 percent of those excess revenues topped off the Rate Stabilization Fund. The rest was there to cover operating expenses and/or perhaps to pre-fund capital.

Under the new methodology, that same year would have overfilled all of the underlying Rate Stabilization Funds to provide that backstop between rate cases because, No. 1, you wouldn't want to have three or four really hot years in a row. We had a drought last year. If we had a drought again this year, we would have a problem, in that we probably wouldn't be generating excess revenues; we would be turning off the ability for people to access water. And so you do have years that fluctuate. And so as a result of this, with the new structure, the fixed revenue going into these buckets will then basically be there as a stabilizer and as monies that can be returned to ratepayers at a subsequent rate case if you had a period of years where you overtopped those Rate Stabilization Funds leading up to that next rate case.

As a point of reference, we have had the 2012 rate case that was required under 11-026 which generated in Settlement a zero percent increase for customers. That zero percent increase included a refund to customers of about $430,000 of excess funds in that Rate Stabilization Fund. So, actually, that was inclusive of that refund to those customers.

Q. And do you have a view as to what would happen if Pennichuck continued to operate under the 11-026 system?

A. (Goodhue) Yes. The Company would be in a position whereby it would be in violation of its line-of-credit covenants at the parent company, and as such would not have the ability to access that facility, but also would be encumbered from accessing any debt for a time for infrastructure replacement and capital needs.

(Court Reporter interrupts.)

A. (Goodhue) The Company would be prohibited from accessing any other debt for its ongoing infrastructure replacement and operating needs.

As is many times the case, a debt instrument like a line of credit has certain covenants and requirements. But also, if you're in violation of those covenants, it has a restriction for the Company incurring any other additional debt.

It would also fall short of its ability to properly service existing debt for principle and interest on an ongoing basis, in that it would have inadequate cash flow over time to properly service that debt.

Q. Does the -- do you believe the structure under this new Settlement Agreement corrects those deficiencies?

A. (Goodhue) Yes, it does.

Q. I'm going to turn to the Settlement Agreement itself and just briefly walk through the structure of it and highlight the terms of the Settlement for the Commission. And starting with Exhibit 4, Appendix A to Exhibit 4 --

MR. HEAD: And for the Commissioners, that's what I handed out as a separate document. I also have extra copies of the Settlement Agreement if that's helpful.

CHAIRMAN HONIGBERG: I mean, we have a copy of the Settlement Agreement.

MR. HEAD: Okay.

CHAIRMAN HONIGBERG: I actually have a question before you go further. Is the Settlement Agreement being marked as an exhibit?

MR. HEAD: We have not marked it as an exhibit separately. We can.

MR. CLIFFORD: Again, it's the -- it would be Exhibit 3. And it is docket book number -- I'm going to have to ask our clerk to --

COMMISSION CLERK DENO: It was filed on the 19th at Tab 26.

MR. CLIFFORD: So we're going to stipulate that Tab 26 in the docket book is Exhibit 3 to this hearing.

CHAIRMAN HONIGBERG: So we're going to mark this Settlement Agreement as Exhibit 3.

MR. CLIFFORD: As 3, right.

MR. HEAD: Thank you.

(Exhibit 3 marked for identification.)

A. (Goodhue) So I believe you were referring to Exhibit 4 of the Settlement Agreement, Appendix A --

Q. Correct.

A. (Goodhue) -- which is Bates Page 51.

Q. In looking at that, just briefly because we've talked about these, just talk about this structure of the three big buckets and what does that mean.

A. (Goodhue) Sure. And I guess just to start, under 11-026, this chart would include just the CBFRR, and then the rest of the allowed revenue requirement would not have as much specificity.

Under the Settlement Agreement, the proposed rate methodology, the approved revenue requirement would be composed of three major buckets: The CBFRR, which is the City Bond Fixed Revenue Requirement; the OERR, which is the Operating Expense Revenue Requirement; and the DSRR, which is the Debt Service Revenue Requirement.

The CBFRR is as defined under 11-026 with a slight modification to the dollars that are elucidated in the Settlement Agreement giving credit to the $5 million for the Rate Stabilization Fund.

The OERR is the component of the revenue requirement in support of the operating expenses of the Company, all the O & M expenses of the Company.

The DSRR is a revenue requirement that is composed of 110 percent of the current debt service of the Company for its external debt, excluding the CBFRR payment from the parent to the City. It's at 110 percent for one simple reason: To provide 100 percent of the cash needed to make those annual principle and interest payments, and 10 percent as an overcover in order to meet the 110 percent EBITDA requirement that is stipulated under the covenant requirements of the bonded debt and the line of credit. And those were actually covenant requirements that we had pushed out as far as we could. Traditionally, lenders will look at 1.25 times or more. We were able to aggressively push down to 1.1, could not get it down to one times only.

The OERR is further broken into two buckets: The MOERR, which is the Material Operating Expense Revenue Requirement, and the NOERR, the Non-material Operating Expense Revenue Requirement. And probably the most simple way to say it is the MOERR are the expenses that would be backstopped by the Rate Stabilization Fund, and the NOERR are the uncovered or unprotected operating expenses allowed in the revenue requirement.

In discussions with Staff and OCA during this case, a number of accounts have been specifically identified as being in that NOERR, as being included in the revenue requirement as adjusted and pro formed in the rate case for the test year, but would not have that Rate Stabilization Fund to backstop them. They are expense items where, you know, prudency is always the case, but, you know, where absolute prudency is concerned, and where management has the responsibility to make sure that we manage within those allowed levels of revenue dollars provided.

Q. And simply by having the NOERR items, does that mean those are non-prudent, or are they still prudent but to be determined later?

A. (Goodhue) They are prudent and to be

determined in each rate case as far as their allowed levels.

Q. You briefly mentioned the 1.1 multiplier and the 1.25 multiplier. In your original testimony with the filing in this case, you had requested and sought the 1.25 multiplier. Can you explain why it is that you've now been able to revise that and bring it down to a 1.1?

A. (Goodhue) Yes. The DSRR is based on the existing debt service for external debt that the Company has in the test year. Between this test year and the next test year, we're going to be layering on annual layers of debt for infrastructure replacement. In my prefiled testimony, we indicated a 1.25 times multiplier for two reasons: No. 1, to make sure we had the EBITDA coverage, but also to provide extra revenues to service debt that would have been incurred in those years between rate cases. However, in my testimony, I also indicated that we would be willing to back that number back down to a 1.1 times multiple to service the existing debt and meet the EBITDA covenant test, so long as we could look at an element similar to the QCPAC, where we could get an annual surcharge allowed for those layers of debt that would be incurred between rate cases, to make sure we had the cash flow to service that incremental debt as that debt was added on for used and useful capital put in place and you've incurred those annual additional principle and interest payments.

Q. And does the structure now that includes the QCPAC provide you with that comfort that you --

A. (Goodhue) Yes, it does.

Q. Turning to the Settlement Agreement itself, on Page 6 and 7, of the revenue requirement portion of the Settlement.

A. (Goodhue) Did you say 6 and 7?

Q. And I'm looking at Bates page numbers. So, turning over to Bates Page No. 7, does Paragraph 1 outline the total revenue requirement that would be part of the Settlement Agreement?

A. (Goodhue) Yes, it does.

Q. And then looking to Bates Pages 28 -- I'm sorry -- Bates Page 9?

A. (Goodhue) Yes.

Q. And looking at Paragraph 4, and I won't read it, but what is the revenue requirement? How does that translate into rates that would be paid by an average consumer for Pennichuck Water Works?

A. (Goodhue) Sure. Under 11-026, or prior to this rate case, we had basically two types of customers for PWW: Those that are subject to the WICA and those that are not subject to the WICA. This case winds up putting all our customers subject to the QCPAC going forward.

Q. So, just to interrupt, so that distinction that you currently hold, with some that are subject to WICA and some that are not subject to WICA, that will go away?

A. (Goodhue) Yes, it will.

Q. And all the customers will be subject to the QCPAC?

A. (Goodhue) That is correct.

Q. Okay. Go on.

A. (Goodhue) So as a result, Paragraph 4 talks about the impact on a residential customer going from an average bill of $50.12 per month to $54 per month. That is the impact on WICA customers, as is indicated where it says $50.12 is inclusive of the WICA surcharge. So that would be the impact on a WICA customer.

For a non-WICA customer, they would be going from a level of $48.65 on average per month to $54 a month, which translates to an annual impact on them of $67.92 as opposed to the $46.56 annual impact on WICA customers.

Q. And then going back to Bates Page 8 on the Settlement Agreement, when would this Settlement become effective? What would be the -- when would it be effective to which bills?

A. (Goodhue) On a bills-rendered basis on or about after December 7, 2016.

Q. That's the correction that was noted earlier?

A. (Goodhue) That is correct. And a very notable correction.

Q. And then looking to Settlement Agreement Bates Page No. 10, this is where the

Settlement begins to discuss the modifications to the ratemaking structure; is that right?

A. (Goodhue) That's correct.

Q. Is that where looking at appendix -- or sorry -- Exhibit 4, Appendix A, this is the text that goes along with that chart?

A. (Goodhue) That's correct.

Q. Okay. And we've talked about it, and I just want to very briefly go through the various elements of that that are outlined in the Settlement Agreement. And you don't need to repeat testimony, but just briefly put it into the structure of the Settlement.

Looking at Page 12 of the Settlement, and if you also have in front of you the Exhibit 4, Appendix A, Bates Page 12 starts with the description of the CBFRR; is that right?

A. (Goodhue) Yes, it does.

Q. And that is what is currently existing under the 11-026 Settlement?

A. (Goodhue) That is correct, yes.

Q. Looking to Page 13, Bates Page 13 of the

Settlement, is that where the Settlement Agreement begins the discussion of the new OERR?

A. (Goodhue) That is correct. This is where you wind up having the modification begin.

Q. And again, what is the breakdown of the two funds of the OERR?

A. (Goodhue) So, basically the OERR is total O & M expenses, and it is broken into two buckets. And it's probably better to talk about the exclusion versus the inclusion.

The exclusion from the expenses that are backstopped by the Rate Stabilization Fund are the expenses that are identified as the NOERR expense items, or the Non-material Operating Expense Revenue Requirement items.

Q. And those are --

A. (Goodhue) On Page 14, Bates Page 14, those accounts are specifically specified and called out.

Q. Okay. And then -- no, never mind.

Looking to Bates page, I think we're on Page 14 now, the DSRR, is that where the Settlement Agreement incorporates the new

DSRR?
A. (Goodhue) Yes, and that is inclusive of the 1.1 times on the annual debt service requirement on existing debt.
Q. And with the DSRR, there's the 1.0 DSRR that has an RSF, and the .1 does not; correct?
A. (Goodhue) That is correct.
Q. And again, briefly, why is that?
A. (Goodhue) It is that the DSRR 1.0, No. 1, are the funds that are needed to actually pay the current principle and interest payments on external debt, and to have that tied to the Rate Stabilization Fund relative to those payments as a stabilizer to insure cash flow to make those payments on a monthly, quarterly or semi-annual basis.
The DSRR 0.1 are revenues that are collected and actually held in a separate bank account to be used on an annual basis as, I'm going to say the "seed money" or initial money in the first couple months of the following year relative to capital that would not have to be bonded by debt because it was already provided for in those monies.

But again, it's really important to understand that the 1.1 is not only about cash flow, but it's about coverage at a EBITDA level for necessary covenants to even access the debt markets.

Q. And again, how is that -- how does that relate to benefits to the corporation and to customers of Pennichuck?

A. (Goodhue) Number 2, absent the ability to meet those covenants, we would not even be able to access the debt markets, number 1.

Number 2, if we could not comply with the covenants, we would be in violation of the terms of those underlying agreements.

And there's also, then, when we sit down with the external agencies, the bond underwriters, the rating agencies, and show them that our revenue requirement is actually tied to an EBITDA generator on a cash flow basis, it gives them comfort that we're going to be able to meet those covenant requirements on a going-forward base.

Q. And just to put it into the structure of the Settlement, you talked about the DSRR 0.1

account as being "seed money." Looking on Bates Page 15 of the Settlement Agreement, towards the end of the long paragraph, is that where that is described about how the one point -- or excuse me. Is that where the Settlement Agreement describes how the 0.1 account will provide "seed money" to the next year?

A. (Goodhue) Yes. And as it states, the Settling Parties agree that any accumulated DSRR 0.1 revenues at the end of a given fiscal year will be utilized as the first funding source for capital expenditures incurred during the first months of the succeeding fiscal year leading up to an annual bonding or financing event in support of capital expenditures for that succeeding year.

Q. And then looking at Bates Page 16 of the Settlement Agreement, does that provide the figures for how the RSF, the three RSF accounts would be initially funded?

A. (Goodhue) Yes. Of the existing $5 million Rate Stabilization Fund, $680,000 will be held in the CBFRR Rate Stabilization Fund; $2,850,000 would be transferred into establishing the MOERR Rate Stabilization Fund; and $390,000 would be transferred into establishing the DSRR 1.0 Rate Stabilization Funds, and $1,080,000 would be held currently in the CBFRR Rate Stabilization Fund pending future transfer to Pennichuck East Utility and Pittsfield Aqueduct Company in future proceedings to establish a similar structure for those regulated utilities.

Q. So, to this point, does the Company anticipate in the next rate cases for the other two regulated utilities that a similar rate structure would be requested for those companies?

A. (Goodhue) Yes.

Q. And then turning back to Exhibit 4, Appendix A, the diagram, can you also briefly describe for the Commission how the Company will manage the flow of money in and out of those RSF accounts?

A. (Goodhue) Sure. And I would also add that not only do you refer to Exhibit 4,

Appendix A, but Appendix B, C, D, E and F. I forget how many letters it is. There's a series of flow charts. The methodology that was established --

Q. Just to clarify, they're not separate appendices but part of the same --

A. (Goodhue) All part of the same exhibit.

Q. Part of that same Exhibit A, labeled "Flow Chart" A, B, C?

A. (Goodhue) All the way up to E.

The mechanism for utilizing the Rate Stabilization Funds and the revenue requirement bank accounts was as established under 11-026, but was established simply for the CBFRR, and the $5 million Rate Stabilization Fund, in that there was a triangular relationship between the main operating account of Company, the Rate Stabilization Fund, and the revenue requirement bank accounts, in that on a weekly basis the pro rata share of collected monies are transferred into the revenue requirement bank accounts. The pro rata share of those revenue accounts are as established on Exhibit 6, which is Bates Page 60 of the Settlement Agreement, which shows those dollar buckets. And the percentage of the hundred -- of the total allowed revenue requirement establishes their pro rata shares. So, whatever their pro rata percentage is on a weekly basis as cash is collected, their percentage is transferred from the main operating account into revenue required bank accounts. At the end of each month, the actual revenues earned in the month are compared with the allowed revenues, which is 1/12 of the annual revenue requirement. To the extent actual revenues are above that requirement, the excess dollars are then deposited pro rata into the Rate Stabilization Funds supporting each of those revenue requirement buckets. To the extent they are deficient, monies are drawn from those Rate Stabilization Funds on a pro rata basis back to the main operating account. Then, as payments are made, whether they're weekly, monthly, quarterly, semi-annually or annually, those payments are made out of the revenue requirement bank accounts. To the extent that monies are insufficient in those accounts, money is transferred from the main operating account into those accounts. To the extent there is excess, it is transferred back to the main operating account. Again, this is a methodology that was established under 11-026 for CBFRR and the Rate Stabilization Fund. It's highly formulaic. It's very specific and very regimented in its application.

Q. Okay. Turning back to the Settlement Agreement itself, Bates Page 18, we've talked about it. This is the section of the Settlement Agreement that implements the QCPAC?

A. (Goodhue) It is.

Q. And again, just briefly describe now what the QCPAC is relative to the existing WICA.

A. (Goodhue) The existing WICA allowed for an annual surcharge just for certain main replacements within the core system of Pennichuck Corporation. The QCPAC is tied to 100 percent of the capital spending for the corporation, used and useful within a year, which is all debt financed. And so based on the debt service for those incremental spends within a year, that debt service at 110 percent to related property taxes for those expenditures are basically established as an annual surcharge request, with the anticipation that for PWW we would be looking at doing an annual bonding event on or about March 1st for the preceding years, 12 months' worth of capital expenditures as used and useful access. And we would then petition the Commission for the approval of that QCPAC later in the year, recoupable back to that March 1st, because as of the date we issue the bonds the requirement to accumulate the monies to actually pay that first interest payment six months after issuance, the clock starts.

Q. And does the filing for QCPAC also incorporate a process for looking forward also?

A. (Goodhue) It does, identical to what was required under the WICA, in that we are not only doing a filing for what was actually being requested from the prior year, but it also includes the current year's budget and an outlook for the years two and three relative to the planned expenditures for the Company.

At the corporation, on our annual budgeting activities with the board of directors of our corporation, as a part of our annual budgeting approval process, we have them review and approve the annual capital budget for that year, but also approve a forecast for years two and three -- so those out years relative to those expense. It approves an overall dollar level, has some specificity as to projects, though the projects will vary over time based on the needs that do exist at that time. And we wind up managing to a number, in that if a project comes on that either wasn't on our radar or comes at a level above, we will then sacrifice another project that might have been on the docket to balance out the dollars relative to those numbers.

Q. So, on the going-forward information, is year one going forward for approval and years two and three informational?

A. (Goodhue) Yes.

Q. And then relative to Mr. Naylor's testimony also, how does Construction Work In Progress relate to the QCPAC? Would that be included?

A. (Goodhue) No, it would not.

Q. So, just used and useful?

A. (Goodhue) Correct.

Q. Is there any -- does the Company have any current plans for pursuing additional debt?

A. (Goodhue) Yes. Our last round of bonding provided funds up through the year 2016. We are preparing at this time a financing petition to be submitted sometime soon for 2017, '18 and '19 capital funds. We've already received preliminary approval from the Business Finance Authority of New Hampshire for the ability to access tax-exempt bonds. That's how we issue it is through their authority. We've already been working behind the scenes with our bond underwriters and our bankers relative to what that means. We have not filed yet, as we needed to make sure that this process had matured enough so that we knew which direction we were headed relative to that proceeding.

Q. Going back to the Settlement, just some miscellaneous terms just to make sure they're in the record.

Bates Page 21 of the Settlement Agreement talks about the withdrawal of the current WICA petition pending. Can you speak to that briefly?

A. (Goodhue) Yes. The Company and the Settling Parties agreed that with the implementation of the QCPAC, that the WICA filing that we currently have in place would then be withdrawn, as it would be replaced by the QCPAC element of this methodology.

Q. And there's a step that's also incorporated into this Settlement?

A. (Goodhue) That is correct. It's inclusive, yes.

Q. Turning to Page 23, Bates Page 23 of the Settlement Agreement, looking at Paragraph small b, have the parties agreed about providing written notice to the Commission about changes in credit rating status with any applicable credit rating agency?

A. (Goodhue) Yes, to the extent we receive anything in writing relative to enhancements or affirmations of our credit rating, we would provide those. I don't always get those in writing, as I indicated to our attorneys. Sometimes it's a phone call just to say, you know, nothing has changed. But yeah, to the extent, certainly to the extent we had an enhancement, we would get something in writing. And upon receipt, and in compliance with this, absolutely we would furnish that.

Q. And on that same page, Bates Page 23, Paragraph small c, is there a monthly reporting relative to the RSFs?

A. (Goodhue) Yes. Again, this is consistent with 11-026, in that we have a reporting element that's relative to that. This is just expanded in compliance with all of the new elements of this rate structure.

Q. Okay. And then on that page, Bates 23, Paragraph d, is that the paragraph that was referred to earlier in Mr. Naylor's testimony about when a new rate case would be triggered?
A. (Goodhue) That is correct.
Q. And what are the thresholds again for that?
A. (Goodhue) If the combined 13-month value of the Rate Stabilization Funds is greater than 150 percent of the targeted amount, then we would be obligated to promulgate a rate case.
Q. And then looking to Bates Page 24, the next page, Paragraph D, how does the Settlement address rate case expenses?
A. (Goodhue) That we agree to file a final rate case expense request no later than 30 days from the date of the Commission's order approving this Settlement Agreement.
Q. And then staying on the same page, is that bottom section of the Settlement Agreement discussing the City of Nashua's eminent domain case?
A. (Goodhue) That is correct. And this is an item of the Settlement that was

clarification relative to any special dividends being allowed as payment to the City out of the regulated utility, prohibiting that.

Q. And based on your experience and your knowledge of this Agreement, in your opinion, is this Settlement just and reasonable and in the public interest?

A. (Goodhue) Yes, I do believe so.

Q. And can you explain why you have that opinion?

A. (Goodhue) I believe that, you know, one of the main concerns we have in running the Company is making sure that not only are we able to provide clean and safe drinking water to our customers, but that we maintain an entity that is financially viable and sustainable for the long term.

As a debt-financed-only corporation, one of the key elements there is making sure that cash flow is adequate to be able to service the debt that is needed to run the Company. I feel that this rate structure is a great result in providing a model that provides the adequacy of cash to meet the necessary operating demands and needs of the Company, provide long-term viability and not designed to create excess profitability to the detriment of customers.

Q. Thank you.

MR. HEAD: With that, that would conclude Mr. Goodhue's testimony.

CHAIRMAN HONIGBERG: Mr. Kreis.

MR. KREIS: Thank you, Mr. Chairman.

DIRECT EXAMINATION

BY MR. KREIS:

Q. My questions obviously are for Mr. Brennan.
Mr. Brennan, would you, just for the record, state your name, your position with the OCA, and briefly summarize what you do in that position.

A. (Brennan) My name is Jim Brennan. I'm the finance director for the Office of Consumer Advocate, involved in utility analysis.

Q. And you participated, did you not, in the negotiation of this Settlement Agreement?

A. (Brennan) Yes, I did.

Q. And you are aware that the OCA is a signatory and, therefore, a supporter of the Settlement Agreement?

A. (Brennan) That's correct.

Q. Now, you heard Mr. Naylor testify at the beginning of the hearing that the Settlement Agreement essentially transforms Pennichuck Water Works into a non-profit company. Do you agree with his characterization?

A. (Brennan) Yes, I agree with that. I think it's important to recognize that PWW, you could view it as entering a new phase, perhaps a third phrase of its transition that started back in 2012 with the Acquisition docket. Those phases have already been summarized with the Acquisition docket. The Company's access to traditional equity markets ended at that point, and with it the benefits of having access to equity ended at that point.

Subsequently, the second part of their transition, as was discussed, is their adoption of a debt structure more in line with acceptability for Wall Street and lenders, where they move toward a fully amortizing debt structure, eliminating balloons, which is positive and leads to good credit ratings, but at the same time rendered the 11-026 model unsustainable and in need of revision, which brings us to this phase of the transition, which is migrating toward a cash-flow-driven revenue requirement model.

Q. You just said "migrating toward a cash flow model." But would you agree that really the Company finds a home? Its migration ends with the adoption of this new model, and really what we're talking about here is a new paradigm; yes?

A. (Brennan) Yes. The Company is -- this transition is maturing significantly with this Settlement Agreement. The benefits to residential ratepayers are strong, in terms of it leading toward lower water rates. What this Settlement and what that rate design does is lowers the Company's cost of capital because the cost of debt is cheaper than the cost of equity. The model mitigates the risk that come with the high leverage that a municipal utility, which PWW is evolving toward, has because the rate structure gives the cash flow stability to service its debt and pay its debt. And the model, because it does support a strong lending model, is leading to, as was discussed, lower interest rates, which is a key benefit of the model.

So, combined, this ratemaking structure of three-part components that cover operating expenses, 0the acquisition debt and the new debt plus the stabilizing factor with the RSF, plus the QCPAC model -- together really improves the credit strength of PWW, and that is a benefit to the customers.

Q. Are you concerned at all that this transition to a rate-setting paradigm that's based on debt service allows any of the Company's expenditures to go unscrutinized or unregulated?

A. (Brennan) No, I believe in the filing the Company has done a good job of documenting how this ratemaking design works in the flow charts. The amount of scrutiny of operating expenses is similar to a traditional revenue requirement analysis. But the design of the DSRR and the CBFRR are exact, highly scrutinized based on the reality of the amount of debt they're borrowing.

Q. You heard Mr. Naylor, I believe, describe the section of the Settlement Agreement that begins on Bates Page 24 of Exhibit 3 as perhaps "the most important aspect" of this Settlement Agreement, and that of course being the part of the Settlement Agreement that has to do with eminent domain expenses incurred by the City of Nashua. Do you agree with what Mr. Naylor had to say about that?

A. (Brennan) Yes, I agree with Mr. Naylor's statements.

Q. Why? Why is that so important from the standpoint of residential customers of the Company?

A. (Brennan) As stated, this model really assumes it's based on covering the cost of PWW for their internal operating expenses, for their acquisition debt and for their ongoing new debt borrowings, and is not intended to generate what was referred to as "excess profits." Essentially, PWW is migrating toward a non-profit-type entity, not intended to bill retained earnings, not intended to upload dividends to stockholders, rather, just to cover its costs, operating expenses and debt service costs.

Q. Looking at Bates Page 10 of the Settlement Agreement, Exhibit 3, there's a sentence there that starts nine lines up from the bottom that says, "While the Commission always retains all jurisdiction and authority to set just and reasonable rates in accordance with the federal and state constitutions and applicable statutes, the Settling Parties agree and reaffirm that the Commission's provision of guidance regarding rate setting with respect to the Penn Corp. Utilities" -- in other words, Pennichuck -- "within the context where they are ultimately owned by the City, is in the public interest."

Do you understand that language as limiting the Commission's authority to regulate this company in any way?

(Witness reviews document.)

A. (Brennan) No, I don't.

Q. And is there anything else that you want to add with respect to the Settlement Agreement being in the public interest?

A. (Brennan) We agree with this Settlement Agreement, the OCA. There were four points in the Settlement Agreement that we advocated for strongly which have already been covered. I won't go through them in detail.

The DSRR 0.1 component I believe is a very favorable part of this, not just for reasons Mr. Goodhue stated, that it covers EBITDA requirements, but actually provides a mechanism for this company to purchase some plant property and equipment without borrowing money. So the DSRR 1.0 pays off existing test year debt. The 0.1 component is basically reducing the amount of debt to some degree for a new plant that's being acquired. And I think that creates a potential, nice dynamic for the company going forward, where that also reduces the QCPAC surcharge requirement as well. So I think that's a favorable part of this docket.

The other items that we advocated strongly for were the bond rating trigger since this design promotes and anticipates strong credit rating to bring down interest costs. And that would be important to know if the credit rating was ever to change.

We agree with the 150 percent RSF triggering a rate case to take a look again at the rate design and also make a decision of what to do with excess fund balance at that time.

And finally, we agree with, on Bates Page 8 and 9, there is a brief discussion of the community water system WICA surcharge or refund that will occur. And we agree with -- these are the non-WICA customers, the non-core customers to handle that surcharge over a 12-month period instead of over a one-month period to avoid any type of rate shock for that particular class of customer.

Q. So, overall, it sounds like a win-win from the standpoint of both the Company and its customers.

A. (Brennan) Yes.
Q. Thank you, Mr. Brennan.

MR. KREIS: Mr. Chairman, those are all the questions I have.

CHAIRMAN HONIGBERG: Commissioner Bailey.

INTERROGATORIES BY COMMISSIONERS

BY COMMISSIONER BAILEY:

Q. Good morning. Can we start with the WICA and the non-WICA customers. This is just something I don't understand. Why would a customer not be a WICA customer?
A. (Goodhue) The way that program was established, it was established for infrastructure replacement with what we call our "core." And so those core expenditures were basically for capital expenditures. And Mr. Ware, I'll look at him -- and correct me if I'm wrong -- just for replacements within the City of Nashua and in the Amherst Village District; is that correct?
A. (Ware) Yes.
A. (Goodhue) So as a result, based on the way that program was designed was based on the

fact that that's where those expenditures were going, those were the customers that were also impacted by the WICA. So it was a limited exposure, as far as what assets qualify. But then those expenditures were also tied to the customers that would be directly benefiting from that. The QCPAC moves us to a mechanism where 100 percent of the capital assets that we deploy, no matter where it would be within the water system --

(Court Reporter interrupts.)

A. (Goodhue) I'm sorry. No matter what those expenditures would be within that system.

Pennichuck Water Works currently services part or all of 11 different communities. And as a result, our expenditures benefit those ratepayers at varying degrees, depending on where a project may be each year or what that capital asset may be. So this is expanding, No. 1, the scope of eligible assets, but also to the benefit of all the customers that are benefiting from it from Pennichuck Water Works.

Q. So Pennichuck Water Works' service territory includes areas beyond Amherst and Nashua?
A. (Goodhue) Yes, it does. Like I say, it's part or all of 11 different communities.
Q. Okay. And have you ever made investments in those other --
A. (Goodhue) Oh, absolutely.
Q. -- communities?
A. (Goodhue) Yes. And under the QCPAC, rather than just being for main replacement work, this includes all of our capital expenditures, which would require pumps, valves, rolling stock, you know, test equipment, maintenance equipment, computer equipment, whatever it might be that is servicing the entire utility. So as a result, if you're funding all of that with debt, and it is benefiting all of your customers, they all should be subject to that surcharge because they're all getting the benefit of it. Our expenditures are not equal within communities on an annual basis. They're on a needs basis. One community might benefit this year and another community

next year, depending on our replacement process.
Q. Can I ask you a question?
A. (Goodhue) Yes, ma'am.
Q. So if the community outside of Nashua and Amherst had an investment under the prior ratemaking scheme, was that not recovered until a rate case?
A. (Goodhue) That is correct.
Q. Okay. In this section of the Agreement that we were just looking at as well, it refers to "refunds or surcharges." My understanding is that temporary rates were set at existing rates.
A. (Goodhue) They were.
Q. And permanent rates are a bit of an increase.
A. (Goodhue) Yes.
Q. So is anybody going to get a refund?
A. (Goodhue) No. No, it's a very, very minor increase -- or a smaller increase for WICA customers and a larger increase for non-WICA customers.
Q. So can somebody tell me why the Settlement was written with respect to "refunds or

surcharges" in a lot of different places? Am I missing something? Bates page 9, 2, it's in three places. And there's other places, but that's one example.

A. (Goodhue) I can only speak to a thought on that, and I'd ask our attorney to confirm.

WITNESS GOODHUE: But inclusive in that rate increase is actually a return of some excess monies from the Rate Stabilization Fund; is that correct?

Q. Well, maybe somebody from the witness panel could answer that.

A. (Naylor) I think that there were a couple of things that were kind of moving targets for us as we were working on this document and putting all the pieces together, one of which was a realization that where we were going away from a return on rate base and going away from depreciation expense, that we needed to deal with the $5 million Rate Stabilization Fund, which was not part of the CBFRR. That was in the Company's rate base, and it was earning a return. That needed to be dealt with in a different way because we were no longer going to be calculating a return on rate base. So the CBFRR for this utility and the other two sister utilities had to be increased slightly to cover that debt service on that additional $5 million. That was a very late addition, as I recall. Some of this language had already been written. And that did cause the rate increase proposed in this Agreement to be a little bit higher than it was.

There was another reason, too, and Mr. Laflamme and I were just speaking of it. It was related to... was it the WICA revenues that we had a question about? Mr. Goodhue alluded to the fact that there is a WICA case pending. It was filed way back earlier this year. It's been held in abeyance because of this case and the potential that we were going to move from a WICA to something else. Those revenues are folded into this case.

A. (Goodhue) Yes, they are.

A. (Naylor) So what we have done is bring all of the 2016 capital expenditures, including the WICA and the non-WICA expenditures, into a step adjustment. That is -- I don't know if that -- in our original calculations if those WICA revenues were part of it or not. But in the stages of drafting, you know, reviewing, working on this document and the accompanying schedules that that language, you know, says refund to customers --

(Court Reporter interrupts.)

A. (Naylor) It's kind of legacy language from an earlier version. So I think that's the reason.

Q. Okay. Thank you.

Can you help me understand, the original $500 million I thought came from the City bond?

A. (Goodhue) Yes. Yes, the City of Nashua borrowed 150.56 million dollars in 2012. Of that 150.56 million dollars, 145.56 was to purchase the Company, and 5 million dollars was to establish the Rate Stabilization Fund.

Q. And aren't you making payments to pay that back?

A. (Goodhue) For the entire 150.56. That is part of the CBFRR payment to the City, yes.

Q. So then the $5 million is already included in the repayment plan.
A. (Goodhue) As Mr. Naylor spoke to, the $5 million was part of the return on rate base as a part of the allowed revenue requirement to provide the cash to fund that total payment. Moving from something that is not a return on rate base to purely something that is tied to the actual revenue requirements for the funded debt, that $5 million now needed to be folded into the CBFRR because we're not getting a return on rate base in the new methodology.
Q. Okay. Can somebody talk about the five-year average test period? Nobody covered that for the next rate case.
A. (Goodhue) Yes, I can speak to it or --
A. (Naylor) Go ahead.
A. (Goodhue) Okay. One of the things again that is there relative to a cash flow basis under a traditional rate setting, you've got a test year and an adjustment for that test year. If you've got a debt equity model, you do have a certain amount of excess profitability

that is just generated from that return on equity prior to 11-026. So, as a rule, we were getting a 9.75 percent return on equity. And we had roughly, you know, 50 percent of our weighted average cost of capital was equity-based. Being a debt-only entity without a return on equity, you can have a year like last year, a drought year. You know, we had revenues that were generous. But what happened is, you know, you go from that year to the very next year, and what it does is just creates a deeper trough relative to your cash flow. So if you looked at last year, and that was the basis for a rate case, you would say your revenues, you're above your allowed revenues and you're fine. But you couldn't file a rate case because you wouldn't show that you were under-earning based on your allowed revenues. However, because everything is debt-based, and your payments there are all related to that debt without a return on equity, without an equity component, you wind up having an exposed level in that very following year relative to

this great swing in your revenues.
So, looking at a five-year trending average as a comparative revenue is giving vision to more normalization of your comparative revenues relative to your cash flow needs, so you don't have these violent swings relative to comparative revenues on a test-year basis.
Q. So you're going to look at the average of revenue over five years.
A. (Goodhue) The preceding five years, the test year and the four years that precede that, as well as the direct costs that are tied to that.
Q. Right. So are the costs being averaged over five years or --
A. (Goodhue) Certain direct costs are, yes, ma'am.
Q. Give me an example of direct costs.
A. (Goodhue) Purchased water, power, purification, okay. So, costs that are really --
Q. Material operating expenses.
A. (Goodhue) And those operating expenses are

the ones that will ride up or down with consumption levels and water production levels, as opposed to certain other expenses like property taxes or wages or insurance, which would be flat, regardless of what revenues are. So I'm going to say that those are the expenses that are most directly tied to variable revenues that ride along with the revenue pattern.

Q.   But do you look at the non-variable -- well, I guess it wouldn't matter because the average would be --

A.   (Goodhue) Those are all based on the test year, yeah.

Q.   Okay. Mr. Naylor.

A.   (Naylor) If I could add to that. If you go to the very top of Bates Page 12, which completes that section on the five-year average, we have written in here to make it clear that, while the Company is going to be using a five-year average test period for computing its revenue efficiency, that does not preclude Staff, OCA or other parties from making an alternative recommendation in place of that with respect to how the Company's revenue deficiency is calculated. So the five-year average, you know, may be useful. It may be very instructive. But we're not precluded from proposing an alternative to it.

Q. So that's what you would expect the Company to file when it files its rate case, the five-year average. And then you'll take a look at that and see if there are any anomalies created by that, and then maybe take a position one way or the other in the next rate case or in future rate cases.

A. (Naylor) Correct.

Q. Okay. Somewhere, and I can't find it -- I can't believe I didn't write the page number down -- there is a phrase in the agreement that says "pertinent adjustments related to financial data." It must be right around that page because that was the next note on my...

A. (Naylor) Looks like it's at the bottom of Bates Page 11, looks like the very last sentence.

Q. That's it. Yeah.
A. (Goodhue) And that would just be to the fact that in any rate case, one of the things that we do is we offer up pro forma adjustments to any of our expenses relative to making sure that items that are of extraordinary nature or not of a normal nature are pro forma in or out, and I believe that's what that's referring to.
Q. And what would "pertinent financial data" include?
A. (Goodhue) Mr. Ware may have an example.
A. (Ware) May I offer up an example?
A. (Goodhue) Well, I can --
Q. Maybe Mr. Brennan will. You're the financial data guy; right?
A. (Brennan) It could be a non-recurring type of expense that you'd want to pro forma. It's not part of an expense you would anticipate going forward.
Q. Okay.
A. (Goodhue) Yeah, something that is a one-off that might occur. I'm trying to think of a good example.

MR. HEAD: Can I ask a question that might clarify?

WITNESS GOODHUE: Sure.

MR. HEAD: Would the Tyngsboro Water System be a relevant --

WITNESS GOODHUE: Yes, that's a perfect example.

A. (Goodhue) So, between rate cases we actually negotiated a water supply contract with a municipality, Tyngsboro, Massachusetts. And that was only partially in effect during the test year. So, in order to really take benefit or to properly account for that was to analyze that on a full year basis, as if that contract was in place for the full year for both on the revenue side and also the expenses related to the supply of the water for that contract.

Q. Oh, okay. So financial data doesn't mean data from the finance industry.

A. (Goodhue) No, no, no.

Q. That's what got me confused.

A. (Goodhue) It's pro forming the actual expenses to give a true reflection of what the actual annual cost of operations would be.

Q. Okay. Thank you. You've answered a lot of questions, so I have to go through my list.

Can you turn to Bates Page 27, please. Can you explain this for me?

A. (Laflamme) Yes. This is a calculation of the revenue requirement that is being proposed in the Settlement Agreement. And it's broken down into basically three sections, mostly -- well, initially it was broken down into three sections to mirror the filing that was made by the Company. And they provided what the revenue requirement would be using the standard test year without a five-year trailing average.

Q. And that would have been a decrease of 1.43 percent?

A. (Laflamme) Correct.

Q. Okay.

A. (Laflamme) And then the next, the middle column is what the permanent rate would be using the five-year trailing average for revenues and expenses. And then the far right column is a calculation of the overall revenue requirement being recommended in the Settlement Agreement, that being $31,496,789. And that incorporates not only the five-year average for revenues and expenses, but also incorporates the proposed step adjustment for the 2016 capital expenditures and also a certain amount of 2017 capital expenditures. And basically the schedule is broken down amongst the three revenue components that were described by Mr. Naylor and Mr. Goodhue, that being the City Bond Fixed Revenue Requirement at the top; secondly, the Operating Expense Revenue Requirement; then third, the Debt Service Revenue Requirement.

Q. And although, if we used traditional ratemaking in this rate case rates would have gone down, you believe that going forward using the new methodology outlined in this Settlement Agreement, customer rates will be less than they otherwise would have been?

A. (Naylor) The biggest driver in the rate increase here is the step adjustment. That first column is just looking at the test year only.

Q. Right.

A. (Naylor) The step adjustment brings the Company up through 2016 with its capital expenditures. And we didn't highlight this earlier, but the Company had two or three very substantial expenditures in 2016, not the least of which was the Company's new operations building.

A. (Goodhue) Yes.

A. (Naylor) and I believe that was about a $7 million investment. Mr. Goodhue is nodding. And a couple of other larger projects. So the Company's total capital spending in 2016 was $19 million. I'm looking at Mr. Goodhue.

A. (Goodhue) Roughly, yes.

A. (Naylor) And he's saying roughly.

So this rate increase that's proposed here is primarily driven by bringing their rates right up through the 2016 year, construction year.

Q. Where their initial filing was through 2015?

A. (Naylor) The initial filing was through test year 2015, yes. But this first column does not include 2016 capital. It does not. Okay. So that's what I thought. And you can see it's a 1.43 decline, call for decrease in rates.

Q. Right. That was my question.

A. (Naylor) Yeah. Yeah, but they hadn't always requested a step adjustment. That wasn't part of the original filing. So that step really is the main driver for the increase.

And I know your question goes to do we think it's reasonable when the test year may call for a slight decrease. And we're proposing an increase in revenues of about 7.6 percent. It's based on capital additions that are completed and in service.

Q. And I assume prudent? Has the Commission decided that they are prudent, or are we deciding that in this case?

A. (Naylor) You are deciding that in this case.

Q. Okay. Do you have an opinion on that?

A. (Naylor) Yes. These have been looked at. And I believe Mr. Laflamme will tell me if the step adjustment assets have been audited. Is that something -- some of them. That's right. The WICA-related ones are audited. And there was an audit report attached to this that's related to the WICA.

But again, proposing this kind of a rate increase is in line with the principles of the Settlement I think in total. We want to get this company up to a level where its cash flows are even with its cash needs. And I think we have done that. The last time, exclusive of WICA, that this company had a rate increase was I believe its 2010 rate case based on the '09 test year.

A. (Goodhue) That is correct.

A. (Naylor) So this company has gone from 2010 through 2016, with a substantial amount of capital investment last year, and the changes to the rate structure that we're proposing here, a 10 percent increase on the debt service 1.1. We have eliminated depreciation lives, and we're giving the Company interest on its debt and principle payments in place of depreciation. Given all of that, it's a 7.6 percent increase in revenues. I think it's very reasonable. And I think it sets the Company on the course that we want it to be on now, as Mr. Goodhue was saying with his task of going out into the market and getting debt. There's nothing else that's more important to the Company than being able to secure debt. There's no equity available.

And so I think in light of everything that we're trying to accomplish here, the rate increase is reasonable.

Q. Okay. Under the proposal, the majority of the RSF will be to insure payment of operating expenses?

A. (Goodhue) Yes, ma'am.

Q. I understand why you need cash to insure that the banks are comfortable that you have enough money to pay your principle and interest. And that was the original intent I think of the RSF.

A. (Goodhue) Correct.

Q. Why is it important to allocate so much of the RSF to insure payment of your expenses?

A. (Goodhue) In Exhibit 6 to the Settlement Agreement, on Bates Page 60 --

Q. All right. Can you give me a -- oh, Bates

Page 60.
A. (Goodhue) Bates Page 60, yes. There is actually the analysis that we have done in support of the required levels of the bifurcation of the Rate Stabilization Fund. It takes into consideration volatility of revenues, as well as operating expenses, as well as the pro rata shares of those buckets. The CBFRR is a fixed-dollar payment that will not change over time. You know, the City issued their debt in 2012 and it matures in 2042, and it is roughly an equal payment on an annual basis.
Q. Before you go on with that --
A. (Goodhue) Yes, ma'am.
Q. So when you originally were acquired by the City of Nashua, you needed $5 million to insure the debt holders that you could manage that debt.
A. (Goodhue) I can speak to that. The analysis that was actually done at that time -- I was not a part of that case specifically, but one of my associates, Mr. Ware, was -- and he was actually the architect for the actual

numerical calculation in support of that $5 million.

That calculation at that time contemplated not just the repayment of the City obligation, but also the coverage of external debt and operating expenses.

Q. Is that what the original Settlement Agreement said? I thought it could only be used for CBFRR?

A. (Goodhue) No, I'm saying how the number, how it was arrived at, how the number was arrived at. So it was a number that had plenty of head room above what was actually needed for the CBFRR payments by themselves.

Q. But you couldn't use it for anything else.

A. (Goodhue) Correct.

Q. So it was just too much money?

A. (Goodhue) Yeah, it was just encumbered just for that in that Settlement Agreement. And I can look him in the face, and I know he did the calculation, and he has told me, chapter and verse, many times that that number was based on a whole lot more than that, but it was restricted for just that purpose.

Q. All right.

A. (Goodhue) Yes, ma'am.

Q. Now you don't need that amount to cover the CBFRR, so you're splitting it up into operating expenses and debt service.

A. (Goodhue) Correct. And it is because, again, as a debt-financed organization, and where cash flow is key, when you have fluctuations in revenue, you not only need to be able to service those fixed obligations, but you need to be able to pay your operating expenses. So as a result, what this structure does is provides stabilization behind all of the necessary financial elements of the Company, those being long-term, which are serviced on an annual basis, or periodically through the year, but those which are on an annual basis, and some may fluctuate with lower than allowed revenues or higher than allowed revenues. And as a result, that is why that is such a large bucket, because when you look on an annual basis, it represents probably 50 percent of our revenue requirements tied directly to those expenses.

Q. Okay. Does the City of Nashua act as a backstop in any way when you're looking to get financed?

A. (Goodhue) They do not. They are solely a shareholder. Their responsibility and authority as allowed under 11-026, and as stated in the Articles of Incorporation of the By-laws of the Corporation are the following: They have the right to elect and re-elect directors as nominated by our Nominating Committee of the Board, and they have the authority to approve any debt that we issue within the corporation. So anytime we issue debt, not only do I have to get my own board to approve the issuance of debt, I also have to file a petition with the PUC if it happens to be debt for one of the three regulating utilities. But I also have to have shareholder approval for the issuance of that debt. So those are their two allowed responsibilities as shareholder. And they have the right to payment relative to the CBFRR back to them in service of the debt obligation.

Q. Okay. Thank you. That's all I have.
A. (Goodhue) Thank you.
BY CHAIRMAN HONIGBERG:
Q. Mr. Naylor, I want to circle back to something Commissioner Bailey asked you about the 2016 expenditures.
Do we have anything in the record other than what you just said about the prudence of those expenditures?
A. (Naylor) Yeah. If we look at the language with respect to the step adjustment... if anybody finds that before I do, let me know.
We are on Bates 7. At the top of Paragraph 1, we are talking about the revenue requirement here and what it's composed of. And we are talking about the step as well. The step increase is the largest driver of the rate increase here, and it's based on '16 and certain '17 plant additions which will be fully in service at the time rates are implemented. And we have the components summarizing --
Q. So we can infer that Staff believes they were prudent by their inclusion in the Agreement?

A. (Naylor) Yes.

And they are going to be audited. If we continue on in Paragraph 2, that indicates that the step adjustment shall be audited by the Commission Audit Staff prior to the implementation of customer rates.

Q. Okay. The circumstance in which a rate case is required, can one of you paint a picture for me as to what will have happened, what course of events will it take to get us to the point where the full rate case requirement will be triggered?

A. (Naylor) Well, I believe you're referring to the 150 percent.

Q. Yeah. What will have happened? How will -- will the Company have stopped borrowing and building and things will just be building up? How will it play out that all of a sudden what appears to be a pretty flexible system will be producing that much money?

A. (Naylor) Well, I guess the sales are going to have to be pretty strong for, you know, two or three years. Although, that's hard to imagine that that's likely. I mean, I think

Mr. Goodhue alluded to this series of very hot and dry years. The revenues aren't going to continue to go up year by year because it's going to impact the supply, and so, therefore, there's going to have to be outside restrictions and so forth that's going to tamp the demand in hot weather.

A. (Goodhue) The other circumstance that might occur is, and I don't know if this is realistic, build-out in the city of Nashua is pretty significant. But if you had a great deal of economic growth perhaps, and as a result revenues elevated because of that, that could cause that to happen. You know, I've talked about how could your revenue base include -- increase within the City of Nashua. Well, you could have neighborhoods within the city that are single-family homes that want to be replaced with multi-family units; so now your consumer density on a footprint could be increased. Or you could have a build-out in some of the communities we serve in those others communities where you have a significant amount of increase in homes and residences and therefore customers, and that could create that. And if you couple that especially with a year or two of really hot, dry and over-abundant consumption, then maybe you could overtop those Rate Stabilization Funds to the point of that 150 percent tipping point where we would need to come back.

Now, why would that be prudent? Well, if your customer base increased significantly, you'd want to have that reflected in your rates going forward. If it was just purely from that water consumption, that's where the five-year trailing average comes in.

Q. Also in that same paragraph, which is from Bates 23 to 24, there's the provision I know has already been alluded to, that the Company will also be keeping records of what things would have been like had not -- if this Settlement were not in place.

Mr. Naylor, wouldn't you find that information interesting, anyway? Isn't that the kind of thing you would want to know about over the course of the next few years, to see if this Settlement has turned out to have made sense?

A. (Naylor) Yes, I think so. The Company has in its first rate case after the acquisition and in this one provided us with data to show what its rate increase request would have been under the old model, under the, you know, debt-equity, investor-owned model. This calls for comparison with the original ratemaking structure from the Acquisition docket. I think it's useful.

I'm confident that what we put together here is going to be clear. It's going to be auditable. The Company will be coming in to visit us every year with a QCPAC. It's going to be providing us with monthly reports on the Rate Stabilization Funds, in addition to statements, traditional statements that they file with us, financial statements. And I think it's significant that the Commission does not -- this does not call for the Commission to give up any of its regulatory authority in any way. The Commission will always have the authority do make alternative decisions with respect to this Company and how its rates are set.

So I think, while that historical information and so forth is useful, I don't know if it's critical information. But we know what we want to do with this. We think we have the right approach going forward. And this certainly puts, this Agreement puts a lot of additional obligations on the Company's management. There's a lot more moving parts. They've got to set up new accounts. They've got to have new tracking mechanisms. So I think we'll have enough ways to monitor what's going on.

Q. Does this structure exist elsewhere?

A. (Naylor) To the best of my knowledge, in what is still ostensibly an investor-owned utility, no.

Q. The very last thing you said echoes something someone said right at the beginning of this hearing, that it is "similar to what goes on in municipal utilities." Is that the analogue here then?

A. (Naylor) Yes. Yes.

Q. What, in you view, are the essential characteristics of this situation that makes this structure make sense? Because I'm kind of interested in whether others are going to be saying, well, I'm sufficiently like this. I have five of the six essential characteristics. Kind of like to know what those essential characteristics are.

A. (Naylor) First of all, this Company has no equity; therefore, there's nothing built into customer rates to provide a return to shareholders. So, in addition to that, and the dividend restrictions that I highlighted earlier, this business exists solely to provide service to its customers. There is no profit-making motive. And to the extent that the Company does have, you know, excess revenues, there are protections in place for those revenues to be used appropriately, and potentially some of them may be refunded back to customers if the Rate Stabilization Funds are overfilled. So I think that's the critical component.

And also, we're matching the Company's cash needs with its cash inflows. That is going to give the Company's credit analysts and lenders a lot of comfort, and they can lend to this company with assurance that the Company has a structure which is sustainable, which provides it with the cash flows they need. We put language in here that kind of talks about that. And it's... we talk about the Commission's providing guidance or something like that. And it's kind of cryptic, but what it means is that Mr. Goodhue can go to his bankers and his credit people and say this gives me what I need, and this should give you the comfort that you need to give me the $9 million or the $29 million or whatever I need for the next three years for my capital investments, and the proof is here. So --

Q. Mr. Goodhue, you want to add something?

A. (Goodhue) Yeah. And I can speak to that exact dialogue. And it's really consistent to what Mr. Naylor said.

In meeting with the credit agencies and

doing the bonding activities in '14 and '15 -- you know, this structure, does it exist elsewhere? Does it look municipal-like? Yes, it does. We were actually hit with the phrase more than once, that we're "neither fish nor foul," when we were talking to traditional lenders. They couldn't even look at us. And where we really came to a point where we could access funds was when they started looking at us as a municipal-like structure. The covenants we actually negotiated in our bond issuances are identical or very similar to covenants that would be for a municipality.

Now, why did they go there? What does a municipality have that we have? They don't have equity components. They're debt-financed, okay, as opposed to going and bonding like we did in the past with balloon maturity debt at different interest rates and a different credit rating. But it was all based on having that equity return in order to be able to provide the cash flow and to be able to access the equity markets. You had to have excess profit to access the equity markets, because what were the equity markets demanding? They were demanding a dividend, okay.

And so this really does speak to that. And Mr. Naylor is correct. When I go to them and I say I've got a rate structure now that, boy, this is more iron-clad than what you saw last time, I suspect a very positive reaction to that when I speak to the credit rating agencies.

Q. It's better than municipals because it doesn't require anybody to make budget decisions within the municipalities about how they're going to spend money in the future or --

A. (Goodhue) It is better in that regard. I can tell you the one area that it is different, and that's where you talk about the cryptic language, is we do not have the ability to change rates on our own. We have to go through a rate-setting process that takes 12 to 18 months to get rate recovery -- i.e, that's why the Rate Stabilization Funds are so important. That's why the QPAC is so important. Because what that does is it takes off the table the overbearing risk of rate lag, rate recovery lag. Because that was also a concern, that, yes, you do have a structure that's there, but it takes you 12 to 18 months to get recovery. This structure takes that and mitigates that to a great extent.

Q. And to that extent, I would tell you I was sitting in my office reading this and looking at the abbreviation that you are using, QCPAC, and in my head I was saying "quick pack" like an instant rate case.

A. (Goodhue) I like that.

Q. Because that's what you're doing. It's WICA on steroids, and it gives you immediate satisfaction; right?

A. (Goodhue) That's correct.

Q. Or close to immediate satisfaction.

A. (Goodhue) Yeah, it's more contemporaneous. And again, one of the key things we asked for is when that QCPAC is authorized, that it's recoupable in cash and in earnings back to the date of the issuance of the debt because, again, that clock starts on the day we issue the debt, as far the cash needed to service that debt.

Q. All right. That's all I have. Does any -- let's go off the record for a second.

(Discussion off the record)

CHAIRMAN HONIGBERG: All right, we're back. Do counsel have questions for their witnesses? Mr. Head.

MR. HEAD: Thank you, Mr. Chairman. One question for-- or a couple questions for Mr. Goodhue.

REDIRECT EXAMINATION

BY MR. HEAD:

Q. Going to the Chair's questions relative to Bates Page 24 about a comparison of the revenue requirements under the Settlement Agreement relative to what would have been required under 11-026, can you speak to that?

A. (Goodhue) Yes. I mean, one of the things we talked about here in this structure is there is a request that the Company agrees to furnish such data to the best of it ability.

The further we get away from 11-026, we're on two different paths, you know. And so to account for that on an ongoing basis would be actually accounting at two different, distinct methodologies, two different abilities to attract financing, Rate Stabilization Funds, how they would be built. So, to account for it on an ongoing basis would be problematic. And what we've agreed is in a rate case proceeding, or based on request, we would pro form what we feel, to the best of our ability, would be the impact of 11-026 versus this current methodology.

Q. So, for example, if you stayed with the current methodology -- or if you were trying to understand what the current methodology would do, would you even know whether or not the bond rating would stay the same?

A. (Goodhue) No, I don't. Again, the further away you get from that mile marker, you're on a diversion path, so some of the certainties go away. There are certain assumptions that have to be brought to bear.

Q. Thank you.

MR. HEAD: No other questions.

CHAIRMAN HONIGBERG: Mr. Clifford.

MR. CLIFFORD: Thank you. I have one question of Mr. Naylor.

REDIRECT EXAMINATION

BY MR. CLIFFORD:

Q. I'd like to point to Bates Page 25, which is Bates Page 24 of the Settlement Agreement. I think this goes to the question asked by the Chair. You see Paragraph 4, Section -- Paragraph IV, 2, discusses about the Commission's acceptance of this Agreement not constituting continual approval of or any precedent regarding any particular principle or issue in this proceeding, and that if any potential order addressing an approval should be granted, that the Commission expressly find that the approvals granted here are really unique to this particular case and not viewed as having any precedential impact. And I just wanted to ask you if it's a fair and accurate statement to say that that, too, is kind of an essential component of the terms of this Settlement Agreement, given the essentially non-equity nature of this Applicant?

A. (Naylor) That is correct.

Q. And I'd like to ask the same question of you, Mr. Goodhue.

Do you view that PWW is essentially a special case, in that this type of ratemaking methodology really is more essentially akin to a municipally -- excuse me -- a publicly regulated municipality, in essence, and that's really the nature of your organization at this stage?

A. (Goodhue) I would agree with that, sir.

MR. CLIFFORD: Okay. Thank you. I have no further questions.

CHAIRMAN HONIGBERG: Mr. Kreis, Do you have anything?

MR. KREIS: I do not.

CHAIRMAN HONIGBERG: I think without objection we'll strike I.D. on Exhibit 3.

[Exhibit 3 I.D. struck and entered as full exhibit.]

Is there anything else we need to do before the parties sum up?

Mr. Kreis, why don't you start us off.

CLOSING STATEMENTS

MR. KREIS: Thank you, Mr. Chairman.

This, from the standpoint of the residential utility customers that the OCA represents, is a really good deal that the Commission should definitely approve. As we've just heard, this company is suis generis, completely unique. And therefore, the parties have worked very well and creatively in their negotiations here to come up with a Settlement formulation that allows the Company to move forward in a proactive and creative way, and in a way that delivers just and reasonable rates. And by "just and reasonable rates," I mean in particular here, rates that are much lower than they would have been had the former paradigm of an investor-owned utility been left in place. I can assure the Commission that had a rate decrease of 1.43 percent of the sort that is featured in the first column on Bates Page 27 been appropriate, we would be here urging you to adopt a rate decrease of that nature. It simply would not be just and reasonable here, given this company's need to meet its debt-service obligations in order to provide the kind of service that its customers expect, and that frankly we expect of it.

There are ample provisions in the Settlement Agreement to assure that the statutory prohibition on putting Construction Work In Progress in rates will be complied with. The Commission hasn't relinquished any of its authority and Staff hasn't relinquished any of its ability and the OCA hasn't relinquished any of its ability to oversee this company and assure that its expenditures are prudent.

Overall, there isn't any -- there is no set of circumstances where I think another company subject to the Commission's jurisdiction could come forward and say, oh, this is a great idea. We deserve something very similar. As I was thinking about the Chairman's question about whether there are other utilities that could line up and say we'd like a deal like this, I scoured my brain, and the only possible analogue I could come up with is the Electric Cooperative. While the Electric Cooperative has a statutory authority to deregulate itself, it also has something that this company lacks, which is full representation of all of its customers and its governing body. So, given that this company has customers who are both constituents of its owner, City of Manchester [sic], and customers who are not constituents, it's completely appropriate as a matter of public policy that this company continue to be subject to plenary regulation. This Settlement Agreement makes clear that that is what this company agreed it will continue to be subject to. And I'm really glad that there was additional colloquy about the reference to the provision of guidance in that regard at Page 9 of the Settlement

Agreement, which is Bates Page 10.

So, given all of this, given the creative work that everybody involved in this docket has done, and given the fact that the result here is just and reasonable rates, I earnestly entreat the Commission to approve the Settlement Agreement that is before you this afternoon.

CHAIRMAN HONIGBERG: Thank you, Mr. Kreis. We heard "Nashua" when you said "Manchester."

MR. KREIS: Ah, I'm sorry.

CHAIRMAN HONIGBERG: Before you go, Mr. Clifford, I'll just note for the record there are no members of the public here interested in providing public comment. There were no intervenors in this case. We did receive I think 12 public comments, the most recent of which was I think received in November on a variety of topics, some of which had to do with water quality, some asking us to examine the rate request very carefully, et cetera. That was the nature of the comments we received.

So, Mr. Clifford.

MR. CLIFFORD: Thank you, Mr. Chairman.

Very briefly, I just wanted to say we started this trip back in November of 2016, and we've had varying degrees of trust or mistrust about what was being proposed. But now that it's obvious, we believe we've made significant progress in this case. Our thinking, as it evolved to accommodate the unique corporate ownership structure, capital structure, and as I've mentioned earlier, I mean, PWW is effectively akin to a publicly regulated municipal utility. And we're going to continue to have -- the Commission will continue to have ongoing oversight.

I echo the statements made by Mr. Kreis on behalf of the OCA. I've also looked on my own to find out if I could find any utility in the United States that's like this, and I could come up with none. So I think we're in an entirely unique situation here in New Hampshire with this utility. And it really is about cash flow matching. And we believe this proposed Settlement is exceedingly just and reasonable and comports in its entirety with the requirements of RSA 378 and really is in the best interest of ratepayers and the utility, and we wholeheartedly support it. Thank you.

CHAIRMAN HONIGBERG: Mr. Head.

MR. HEAD: Thank you.

As everyone has said, we are in a unique situation. And what we've learned since the 11-026 order was issued is significant and important relative to what brings us here today. The 11-026 methodology, as Mr. Goodhue and the others testified to, provides many, many benefits that has put the Company in the position where it is today, which is stronger and in a better position to provide quality service at lower rates that it would have been able to if it was an equity-based company. But we've also learned that the 11-026 methodology has significant restrictions, that if it were to continue would result in significant detriment both to the Company and the customers, especially in terms of cash flow and management of debt, which brought us to the filing of this petition and the request for a change of methodology.

And Staff and OCA are to be commended, in terms of their willingness to explore the issues and concerns that the Company has raised, and also to be very creative and flexible in coming up with this new structure that we have presented today in this Settlement. The Settlement provides unique benefits for the Company and for its customers in its ability to obtain debt financing and to be able to do so at lower rates, we expect, and hopefully with an improved bond rating.

Overall, as the testimony was presented, and as all parties have agreed, this is in the public interest and is just and reasonable, and we strongly request or recommend the Commission approve the Settlement.

CHAIRMAN HONIGBERG: All right. Thank you all. If there's nothing else, we will take the matter under advisement and issue an order as quickly as we can.

(Whereupon the hearing concluded at 12:35 p.m.)

C E R T I F I C A T E

I, Susan J. Robidas, a Licensed Shorthand Court Reporter and Notary Public of the State of New Hampshire, do hereby certify that the foregoing is a true and accurate transcript of my stenographic notes of these proceedings taken at the place and on the date hereinbefore set forth, to the best of my skill and ability under the conditions present at the time.

I further certify that I am neither attorney or counsel for, nor related to or employed by any of the parties to the action; and further, that I am not a relative or employee of any attorney or counsel employed in this case, nor am I financially interested in this action.

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Susan J. Robidas, LCR/RPR
Licensed Shorthand Court Reporter
Registered Professional Reporter
N.H. LCR No. 44 (RSA 310-A:173)

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