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**BEFORE THE NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION**

DW 11-026

In the Matter of:

**City of Nashua & Pennichuck Corporation, et. al.
Joint Petition for Approval to Acquire Stock
of Pennichuck Corporation**

Testimony

of

Fred S. Teeboom

Intervenor

4 September, 2011

INTRODUCTION

1 **Q. Please state your full name and address.**

2 Fred S. Teeboom. My address is 24 Cheyenne Drive, Nashua, NH 03063. I have resided at
3 that address for over 39 years.

4 **Q. Who is your employer?**

5 I am retired.

6 **Q. Please summarize your education and professional work experience?**

7 I hold a Master of Science (MS) Degree in Electrical Engineering from the University
8 Southern California. I worked for over 43 years as a System Research and Development
9 (R&D) Engineer and Senior Technical Consultant on a large variety of government and
10 commercial projects.

11 **Q Do you have government service experience?**

12 A. I was elected twice to the position of Alderman-at-Large in Nashua, in 1993 and again in
13 2005.

14 **Q. Do you have community service experience?**

15 A. I served as President of the Nashua Taxpayers Association. I was the architect and Lead
16 Petitioner of a formal RSA 49-B citizen's petition drive that ultimately resulted in Nashua
17 citizens voting a Spending Cap into its city charter that has been local law for over 17
18 years. I also filed a brief and addressed the NH Supreme Court as Amicus Curiae
19 supporting the legality of local communities adopting spending caps and tax caps.

20 **Q. Do you have water utility experience?**

21 A. No, other than participating as Intervenor in PUC Docket DW04-048 and later as alderman
22 concerning the Eminent Domain acquisition of Pennichuck Water Works.

23 **Q. Do you have financial management experience?**

24 A. I have managed the cost, schedule and performance of multi-million dollar contracts.

1 Q. Are you paid for your effort as Intervenor?

2 A. No, I am probably the only person actively engaged in this case who does not get paid.

HISTORICAL INTEREST

3 Q. What is your interest in the acquisition of Pennichuck Corporation by the City of Nashua?

4 A. I became concerned with the successful initiative by Pennichuck Corporation to form
5 Southwood Corporation as an unregulated subsidiary, carving out for development of what
6 had for many years been protected and fenced-of water conservation land. My research
7 into that process showed collusion between private and government interests, culminating
8 with the transfer of 1,088 acres buffer zone and conservation land to Southwood
9 Corporation for commercial development for about thirty-six dollars (\$36) per acre.
10 Southwood Corporation sold 796 acres of that land between 1984 and 2000 for an average
11 price of twenty-thousand dollars (\$20,000) an acre, creating enormous windfall profits for
12 Pennichuck Corporation.¹ The ratepayers did not benefit from these profits through rate
13 offsets, but have since been burdened with paying for the development of a new \$50
14 million water treatment plant.²

15 Q. Have you opposed the Pennichuck Acquisition?

16 A. The land transfer to the unregulated Southwood subsidiary became a centerpoint in the
17 campaign for mayor of Nashua in 1999, which I actively supported. When Pennichuck
18 Corporation announced its merger with Philadelphia Suburban, the newly elected Streeter

¹ See Exhibit 4. Then-mayor of Nashua Maurice Arel resigned after the NH PUC and the NH Supreme Court affirmed the transfer of conservation land to Southwood Corporation for real estate development, to become the next CEO of Pennichuck Corporation in 1984. Later CEO Arel became subject of civil fraud charges filed by the US Security and Exchange Commission (Case No. Civil-04-475) and by the NH Bureau of Security Regulations (Consent Order INV. 02-029 in 2004), settled with large fines and Mr. Arel's forced resignation in August 2003.

² The prevailing attitude expressed in the Sasaki Report (Reference 1) sponsored by Pennichuck Corporation, is that if Pennichuck builds a water treatment plant to meet new Safe Water quality standards imposed by the federal EPA, then it could convert part of the 2,000 acres of historically held water buffer and conservation land for development. Implicit in this "trade" would be that profits from such sale would pay for the water development plantbut that was not suggested in the report, nor mandated by the NHPUC, nor ordered by the NH Supreme Court on appeal.

1 administration, alarmed by the sale of the water company to an out-of-state organization,
2 offered for the City of Nashua to purchase the company as a publicly owned utility.³ The
3 city arranged a citywide special election on 14 January 2003.⁴ By a count of 6,525 to 1,867
4 Nashua voters authorized the city to acquire all or a portion of the water company.

5 **Q. Did you not take the city to court?**

6 A. I filed a pro-se Writ of Mandamus in Hillsborough Superior Court on 24 December 2002.⁵
7 The City had refused to publish Pro and Con arguments as required under its city charter
8 for a city-wide petition drive, thus slanting the information. For example, the cost and
9 complexities of a hostile takeover through Eminent Domain was ignored during the
10 campaign leading to the vote, and the fact that a RSA 38 process must be limited to the
11 portion of Pennichuck Corporation located within the city (plus dependent pipes and pump
12 facilities outside the city), was downplayed. Thus I believed the citizens were denied a
13 balanced exposition of the facts to guide their vote.

14 **Q. Did you later become an Intervenor in the predecessor Docket, DW 11-048.**

15 A. Yes. I also made my opposition a centerpiece in my campaign for election to Alderman-at-
16 Large in Nashua in 2005, and continued to actively oppose the Eminent Domain process
17 following election.

18 **Q. What was your view on the PUC Determination on DW 04-048 that it was in the**
19 **Public Interest for the City of Nashua to acquire the company, for a cost of \$203**
20 **million, plus a Mitigation Fund, for a total of \$243 million?**

21 A I thought it was a bad decision that ignored the PUC staff's recommendation that the
22 acquisition was contrary to the Public Interest, and set an outrageously high cost for only

3 City officials announced an offer of \$121 million, which they said was equal to the Philadelphia Suburban deal because it includes \$15 million to cover the company's tax liabilities.

⁴ Resolution R-02-127 adopted 26 November 2002.

⁵ Hillsborough County Superior Court Docket 02-E-0441, Fred S. Teeboom v. City of Nashua, decided 6 January 2003.

1 part of the company.

2 **Q. Did you get involved in the Special NH Legislation to permit a 100% stock purchase?**

3 A. Yes, I opposed Eminent Domain, but supported a stock purchase for the entire company.

4 In my consistently held opinion, if the city wants to acquire its water company to preserve
5 conservation land from development, or if the residents fear pollution of the drinking water
6 in favor of profits if the water company that is owned by interests outside the state, then
7 buy the whole corporation. Especially when large conservation land tracks fall outside the
8 city of Nashua that cannot be acquired under the RSA 38 Eminent Domain process.

FINANCIAL CONDITIONS OF THE PROPOSED MERGER AGREEMENT
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9 **Q. Are you pleased with the acquisition cost of the proposed Merger Agreement before**
10 **the PUC under DW 11-026?**

11 A. No. The city had broken off negotiations in 2009, but in 2010 announced that a new
12 agreement had been reached for 100% stock purchase. I examined the cost of \$138 million
13 for the stock at \$29 per share, the high transaction and financing costs (including legal and
14 consulting fees of \$10 million), and the assumption of debt for a total acquisition cost of
15 \$220 million, and determined that to be too high (see Exhibit 1). A better price than the
16 \$243 million set by the PUC for only part of the company, but still much too high.

17 **Q. What would you consider a fair price?**

18 A. The city's consultants had announced in 2009 a fair price for the stock of \$25 per share, so
19 that would result in a \$119 million price instead of \$138 million.⁶ I do not believe the
20 ratepayers should be held responsible for \$5 million spent by the city on the predecessor
21 Eminent Domain. I also do not believe a \$5 million Rate Stabilization Fund should be
22 established to underwrite the cash payments (CBFRR) due the city. Thus the acquisition

⁶ The city announces on 8 December 2009 that its investment banking consulting firm determined Pennichuck Corporation's fair market value, including a reasonable premium, to be \$25 per share, not the \$31 Pennichuck had floated. Mayor Lozeau ordered termination of further negotiations.

price of \$157 million (excluding debt assumption) should be reduced by at least \$29 million, to \$128 million, which comes closer to the \$121 million offered by originally.

Q. Are you pleased with the financing arrangement of the proposed Merger Agreement?

A. No. This acquisition is 100% leveraged. Every penny for this acquisition must be borrowed over a period of 30 years with general Obligation Bonds, not Revenue Bonds.⁷ This new debt must be repaid with water revenues. If water rates revenues fall short, the taxpayers of Nashua are solely responsible to make up the remainder of the debt payments. The 100% leverage position is certainly in variance with the Rizzo Report , which defines a desired mix for a water utility to consist of 40-50% equity, not 0% equity (capital) and 100% debt (see Reference 2).

Q. Are you not persuaded that the debt payments will be fully paid with water revenues?

A. No. Payment on new debt of \$157 million, under the assumption that the assumed long term debt (see Exhibit 1) will be assumed under current terms, comes to \$11 million annually for 30 years, in equal payments at the assumed rate of 5.6%. This cannot possibly be paid entirely from current revenues, even assuming the projected operational costs drop by nearly \$2 million, and no dividends need be paid to shareholders (about \$4 million). In the proposed scheme, the subsidiary regulated water companies (PWW, PEU and PAC and the unregulated companies (Southwood and the Water Service Company) pass all tax liabilities and depreciation dollars to the “holding” corporation, which defers tax payments and uses the cash to pay the debt, while depreciation is replenished with additional borrowed capital expenses. Exhibit 3, produced by the Petitioners, illustrates the negative cash flow condition that must be made up from the proposed Rate Stabilization Fund,

⁷ This is a significant distinction. The taxpayers of Nashua are responsible for the General Obligation (GO) bonds, whereas Revenue Bonds are paid exclusively through proceeds from utility water sales. During the 2003 Special Election, the voters were specifically assured, through the language of enabling resolution R-02-127, that the acquisition would be paid with Revenue Bonds, not GO bonds.

1 entirely funded with additional borrowed money.

2 Q. **The consultants produced numerous spreadsheets to demonstrate that the retained**
3 **earnings will be sufficient to reimburse the city for the annual debt payment.**

4 A. The consultants who prepared these spread sheets work for C. W. Downer, an international
5 investment firm who specializes in “finding opportunities” for mergers and acquisitions.
6 These consultants are wizard at producing spread sheets that take advantage of every
7 possible federal tax loophole, that can convert losses into gains and that can justify just
8 about any acquisition, given assumption of large debt. The barrage of complex
9 interlocking spread sheets produced for the Pennichuck acquisition is no exception.

10 Q. **Are you saying these analyses are dishonest?**

11 A. No, I am saying that they are contrived to produce the favorable result the client desires.
12 In the Pennichuck situation, they produce spread sheets to show that new annual debt
13 payments of \$11 million can be incurred and sustained, while keeping rates “below
14 Pennichuck private ownership.” Of course, they go through the usual gyrations of
15 depreciation and interest payments and investment credits offsetting any earnings so that all
16 federal taxes and state taxes get deferred, borrowing constantly against expenses, etc. In
17 short, the very financial manipulation that ultimately grows into stratospheric unsustainable
18 debt that can ultimately produce a financial meltdown example. The charts in Exhibit 2,
19 extracted from a 30-year financial analysis produced by C. W. Downer for the City of
20 Nashua, illustrate the financial manipulations. For example, as the acquisition debt is paid
21 off, borrowed money to cover 100% of capital expenses takes its place. Presumably, after
22 30 years the \$157 million acquisition debt is paid off, and then the accumulated capital
23 expense debt can be paid off...if cool heads prevail.

24 Q. **Could you provide an example?**

25 A. Certainly. Capital expenses are constantly borrowed, constantly grow. When I questioned

1 this during a technical session the response was, “for utilities, all capital expenses are
2 highly leveraged, for capital expenses are granted a higher rate of return than equity.”
3 Translated, that means the PUC will grant you 9.75% rate of return on money you borrow
4 at 5.5%, so you should borrow as much as you can.⁸ Why sell stock when you can make a
5 profit on borrowing? Total debt, the consultants claim, do not really increase if you
6 consider the effect of inflation. Furthermore, borrowing delays increasing rates, thus the
7 claim can be made, ‘rates under city ownership fall below Pennichuck ownership.’ Best
8 of all, the city will guarantee payment on debt if the company cannot meet those payments.

9 **Q. So if good for the industry, why not good for government**

10 A. Because government cannot raise equity when cash is needed that cannot be raised with
11 water rates or through more borrowing, by selling shares of stock. Government has to raise
12 cash through taxation that falls on everyone.

GOVERNANCE UNDER THE PROPOSED MERGER AGREEMENT

13 **Q. Do you approve of the ‘Plug and Play’ organization of the proposed Merger Agreement?**

14 A. I understand the mayor’s argument that independence from politics while keeping the current
15 experienced management team and employees in place is good for running a water
16 company, and better than bringing in a new management team like Veolia and Beck, with
17 new employees. I am concerned about the proposed organization, arranged behind the closed
18 doors of non-public meetings, which calls for excessive independence by a self-appointed
19 board of directors, very limited public oversight, a for-profit corporate status, all in near-total
20 variance of what had been represented over the years in public arguments to be the benefit of
21 public ownership of the water company.⁹

⁸ See Exhibit 4, from attachment to Response to OCA 2-4(a), 25 April 2011

⁹ Except for enumerated “Reserved Powers,” in the Bylaws, the Board has the same independence of operation as under private ownership.

1 Q. Do you approve of the “for-profit” status of the new corporation proposed under the
2 Merger Agreement?

3 A. No. The argument is made that the combined federal and state tax liability is \$45 million, and
4 that would cause the annual new debt payments to increase by \$3 million, from \$11 million to
5 \$14 million, given the same terms. There are two problems with that. First, a tax-exempt
6 bond for a non-profit is lower by at least 1% compared with a taxable bond for a for-profit
7 corporation. But more significant, a non-profit corporation pays no federal and state taxes.
8 The C.W. Downer spreadsheets produced for the PUC only carry only 10 years of the 30-year
9 period of the acquisition bond, so the effect of taxes are masked by the deferred taxes of those
10 early years (See Chart #3 of Exhibit 2). The C.W. Downer consultant claims that a “call”
11 option allows conversion of the bond after 10 years, if it is advantageous to convert to non-
12 profit status. But a trade-off was not presented by C. W. Downer, claiming the “variables for
13 prediction are too great.”

INVENTORY OF ASSETS ACQUIRED UNDER THE PROPOSED MERGER AGREEMENT

14 Q. Are you not pleased that at least no more conservation land will be sold off?

15 A. In fact, land continues to be sold off. The Merger Agreement contains a “Parcel F” that
16 consists of about 33 acres of conservation land and wetlands next to a water reservoir
17 abutting Concord Street that was under agreement to be sold under a P&S agreement
18 between Southwood Corporation and a local development firm, pending Nashua Planning
19 Board approval. The details of that sale were not made public, and from the minutes, not
20 made known to the aldermen prior to their vote to authorize and fund the acquisition. That
21 sale could and should have been removed from the Merger Agreement

22 Q. Do you have an inventory of what is acquired with the acquisition purchase of \$157
23 million?

1 A. No. A detailed inventory has not been produced, identified in the proposed Merger
2 Agreement. The Sasaki Report (ref. 1) and Rizzo Reports (ref. 2) contain detailed
3 inventories, but no such inventory has been made public to my knowledge. None was
4 included under that the heading Company Disclosure Schedule in the Merger Agreement

5 **Q. Do you have a clear definition of any contaminated sites?**

6 A. A list has not been produced. Frankly, I have no idea what Nashua is buying for \$157
7 million of taxpayers' money and \$63 million of assumed debt.

8 **Q. Are you at least pleased with the fact that after 30 years** the acquisition debt will be
9 paid off, and the water rates should drop drastically.

10 A. Yes, as long as all of the borrowing to pay for the acquisition has not exceeded the original
11 obligation, which is a big question mark. The consultants justify all borrowing to be
12 devalued by inflation. That is like saying that the federal debt of over \$14 trillion is not
13 alarming, for adjusted for inflation that would have amounted to "pocket change" projected
14 back to Alexander Hamilton.

15 **Q. How about the fact the water company will be fully owned by the city**

16 A. I am not favorably disposed to public ownership of anything the private industry can do.
17 But considering the sordid history of greed and corruption in selling off conservation land I
18 earlier cited that has been the history of Pennichuck Corporation, in this instance that is a
19 definite bright spot in this acquisition saga.

NHPUC ABILITY TO EVALUATE THE PROPOSED MERGER AGREEMENT
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20 **Q. Do you believe the PUC can make a fair determination of the public Interest?**

21 A. The PUC has already determined that ownership of the Pennichuck Water Works is in the
22 Public Interest, in the Eminent Domain Docket DW 04-048.

23 **Q. Do you think the PUC can set a fair valuation as to the price for the acquisition?**

1 A. In DW 04-048 the PUC set a price higher for part of the company (\$234 million) than is
2 now proposed to be paid for the whole company of \$220 million, including transaction fees
3 (see Exhibit 1). From the staff questions I have seen, none appear concerned about
4 corporate governance structure, the proposed for-profit tax status of the new corporation
5 and the implication thereof on future rate increases, or the city's ability to pay the debt on
6 its General Obligation bond.

7 Q. **Do you think the PUC can set a fair value as to water rates?**

8 A. The PUC rate setting formulas, as I try to understand them, do not lend themselves to a
9 100% leveraged stock acquisition; 100% borrowed money and 0% equity. The PUC
10 allows 9.75% markup on capital expenses, whereas the true cost of borrowing is between
11 5% and 6% (see Exhibit 4). The extra allowance is supposed to form a hedge. But in
12 addition, the Petitioners want a \$5 million renewable Rate Stabilization Fund, to form an
13 added hedge. I don't think you can get it both ways.

14 Q. **So how do you propose the PUC sets the water rates?**

15 A. I do not have the requisite knowledge to advise the PUC on setting rates, when the buyout is
16 100% leveraged and no equity exists.¹⁰ No primer is available on how that is done, for I had
17 inquired with Mark Naylor, a PUC staff economist advising in this docket.

RECOMMENDATIONS CONDITIONAL TO APPROVING THE PROPOSED MERGER AGREEMENT

18 Q. Do you have recommendations conditional to the PUC approving the Merger Agreement?

19 A. Yes. Let me summarize eight recommendations:

20 **1. Reduce the premium in the acquisition price paid for the stock**

21 The "premium" paid for the stock is effectively \$6.00, or between 26% to 40% on stock

¹⁰ The Municipal Acquisition Regulatory Asset (MARA) proposed by the Petitioners is an accounting scheme to get around debt to-equity ratio limits set by current Pennichuck Corporation lenders, when the city's acquisition has no equity, only debt.

1 that for many, many years traded between \$19 and \$23.¹¹ The mayor announced in
2 December 2009 that the maximum value for the stock should not exceed \$25.00. The
3 acquisition price should be reduced to \$25.00 per share, a reduction of \$19 million.

4 **2. Do not charge the ratepayers with legal and consultant costs.**

5 The acquisition include legal and consultant costs of \$5 million the city paid for its
6 now abandoned Eminent Domain case (DW 04-048), and another \$5 million legal
7 and consultant costs to pay for the current acquisition (DW11-026). These costs
8 should not be carried by the ratepayers, many of whom never voted for this
9 acquisition, within and without the city of Nashua. This should be carried by the
10 city's taxpayers who now own the company, resulting in a further reduction of \$10
11 million (see Exhibit 1).

12 **3. Order a complete inventory of the acquisition be made public.**

13 Order a complete inventory, including identification of all contaminated sites,
14 Superfund sites if any, the pollution condition in all reservoir/retaining ponds/natural
15 springs, the condition of the Nashua filtration plant and the condition of the water
16 distribution system including water pipes, water towers and pumping stations, as a
17 condition of approving the acquisition

18 **4. Stop "back-door" sales of conservation land.**

19 Order the 33 acres of conservation and wetlands identified as Parcel F on Concord
20 Street that were not publicly announced prior to the aldermanic vote authorizing the
21 acquisition, and currently not developed, be terminated as a condition of approving
22 the acquisition.

23 **5. Change the proposed "for-profit" corporation to a "not-for-profit" corporation.**

24 The Merger Agreement calls for the newly formed corporation to be established as a

¹¹ The share price shot up shortly after the Merger Agreement was announced, near the \$29 agreed price.

1 ‘for-profit’ corporation, to avoid a \$45 million tax liability. It is not clear this
2 liability applies to assumption of a taxable corporation by a municipality, but even if
3 it does, it is entirely dubious this cost amounts to \$45 million (see Exhibit 6).

4 In all public discussions has been the assumption that a new water company, whether
5 folded into the city’s Public Works Division or formed as a separate entity, would be
6 non-profit, so the ratepayers would not be held liable for federal and state taxes. The
7 long-term financial effects of a for-profit corporation in terms of ratepayers paying
8 federal and state taxes and certainly paying higher borrowing costs for taxable bonds
9 has been ignored in the filings, and downplayed in the responses.¹² The PUC should
10 order that the organization be established as a not-for-profit corporation, in the Public
11 Interest. The ratepayers should not be burdened with any tax liability, whether \$45
12 million or less, but should be given the full benefit of the financial advantages of non-
13 profit status of public ownership.¹³ If non-profit, full disclosure need be made of
14 “payments in lieu of taxes” agreed to be paid, if any, to communities that would lose
15 tax revenues currently paid by Pennichuck Corporation.

16 **6. Full disclosure of revenues from municipalities under public ownership.**

17 Currently the city of Nashua and other communities pay for water services associated
18 with fire protection, such as large diameter water supply pipes and fire hydrant
19 maintenance. Under public ownership, any such revenue projections must be
20 disclosed from all communities receiving such services, including the city of Nashua

21 **7. Review the proposed corporate independence**

¹² The “for-profit” corporate argument has been exclusively based on the claimed \$45 million tax liability to be incurred by the city with its acquisition cost, without a detailed analysis of long-term tax and financial implications on the ratepayers after the acquisition is concluded. The Petitioners presented a 30-year financial projection for the city of Nashua, but not for the PUC, so the full implication of taxable status was not presented to the PUC.

¹³ The city’s bond counsel has not provided a written opinion whether the city’s GO bonds to fund the acquisition qualify for tax-exempt rates.

1 The board of directors of the proposed for-profit corporation has an exceptional
2 degree of independence, even as the corporation is wholly owned by the city. For
3 example, it sets its all salaries and bonuses in the corporation, and makes all of its
4 own appointments after an initial 2-year period of operation. A review needs to be
5 made of the proposed articles of agreement and bylaws to ascertain whether the
6 corporate independence is too far removed from public control and oversight.

7 **8. Combine the three corporate components PWW, PAC, PEU and Water Services**
8 **into a single corporation; disband Southwood Corporation.**

9 The several independent subsidiaries reporting to a single “holding company” creates
10 unnecessarily complex accounting difficulties, and is not necessary under the sole
11 ownership by the City of Nashua.

12 Q. **If these conditions are ordered by the PUC, will you agree with the proposed acquisition?**

13 A. Yes

14 Q. Does that conclude your testimony?

15 A. Yes

THIS CONCLUDES THE TESTIMONY OF INTERVENOR TEEBOOM
