

STATE OF NEW HAMPSHIRE
BEFORE THE
NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION

PENNICHUCK EAST UTILITY, INC.

DW 13-126

NOTICE OF INTENT TO FILE RATE SCHEDULES

PRE-FILED DIRECT TESTIMONY

OF

JOHN L. PATENAUDE

MAY 2013

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Introduction and Purpose of Testimony

Q. Please state your full name and business address.

A. My name is John L. Patenaude. My business address is Pennichuck Corporation,
25 Manchester Street, Merrimack, New Hampshire 03054.

Q. How are you currently employed?

A. I am currently the Chief Executive Officer of Pennichuck Corporation (Pennichuck)
and the Chief Executive Officer and President of Pennichuck Water Works, Inc.
(Company). I have served in this capacity since January 27, 2012.

Q. Please explain your work experience and educational background.

A. From June 2010 to January 2012, I served as an advisor to the City of Nashua, New
Hampshire (City) as the Transaction Executive, with respect to the merger transaction
between the City of Nashua and Pennichuck Corporation. Prior to serving the City of
Nashua, I worked in several financial positions for various corporations. Until
September of 2009, I served as the Vice President-Finance, Chief Financial Officer and
Treasurer of Nashua Corporation. Prior to that position, other positions held at Nashua
Corporation included Assistant Treasurer and Director of Taxes. Prior to joining
Nashua Corporation in 1991, I worked in various financial capacities for various
companies. These companies included Coopers & Lybrand, Ausimont, N.V., Sanders
Associates Inc. and John Hancock Mutual Life Insurance Company.
I received a B.S. degree in Accounting from Boston College and a Masters in Taxation
from Bentley College.

Q. What are your responsibilities as the Chief Executive Officer of Pennichuck?

25 A. As the Chief Executive Officer, I am responsible for overall management of the
26 corporation, and I report to the Board of Directors. I work with the Chief Operating
27 Officer, the Chief Financial Officer, the Director of Human Resources and the Director
28 of Information Technology to implement short and long term strategies, insure funding
29 of debt and minimize water rate increases.

30 **Q. What is the purpose of your testimony?**

31 A. The purpose of my testimony is to provide information relative to the Pennichuck
32 Corporation merger, corporate governance after the transaction, the cost of the
33 transaction, the interest rate on the City Acquisition Bonds and, compliance with the
34 terms of the Settlement Agreement approved by the Public Utilities Commission in
35 Docket No. DW 11-026 (Settlement Agreement).

36 **Q. Would you please identify the other witnesses in this case?**

37 A. In addition to my testimony, the following witnesses will provide testimony. Donald
38 Ware, the Chief Operating Officer, will provide testimony as to operations. Larry
39 Goodhue, the Chief Financial Officer, Controller and Treasurer, will provide testimony
40 relative to finances. John Boisvert, the Chief Engineer, will provide information
41 regarding capital expenditures.

42 **The Merger Transaction**

43 **Q. When was the merger transaction completed?**

44 A. The merger transaction was completed on January 25, 2012, when the City of Nashua
45 acquired the shares of Pennichuck Corporation.

46 **Q. The Settlement Agreement estimated the "Acquisition Cost" to be \$152,099,885.**

47 **What was the actual acquisition cost?**

48 A. The actual acquisition cost was \$150,570,000. A comparison of the estimated cost
49 compared to the actual cost by category is attached as Exhibit JLP-1. Mr. Goodhue will
50 discuss the major differences in his testimony.

51 **Q. A condition of the merger approval was that the true interest cost of the City**
52 **Acquisition Bonds would not exceed 6.50 percent per annum. What is the true**
53 **interest cost?**

54 A. The true interest cost on the City Acquisition Bonds is 4.09 percent per annum as
55 shown in Exhibit JLP-4.

56 **Q. Can you provide an update as to the governance of Pennichuck after the merger?**

57 A. After the acquisition, the Pennichuck Board of Directors was reconstituted with 10 new
58 members appointed by the Sole Shareholder, the City of Nashua. There were six
59 members from Nashua, including the Mayor; one member from Londonderry; one
60 member from North Conway; one member from Windham; and, one member from
61 Amherst. These individuals also serve as members of the boards of directors of
62 Pennichuck's utility subsidiaries.

63 As agreed to in the Settlement Agreement, the By-Laws of Pennichuck Corporation
64 require that one member of the Pennichuck Corporation Board of Directors be
65 nominated by the Merrimack Valley Regional Water District. The District has
66 nominated a member who is currently being considered by the Board of Directors. If
67 approved, the Pennichuck Board of Directors will recommend the nominee to the Sole
68 Shareholder for approval.

69 While the Pennichuck Board members are from different locations, they have a
70 fiduciary responsibility to care for the finances and legal requirements of the

71 corporation. They must act in good faith and with a reasonable degree of care. The
72 interests of the corporation must take precedence over personal interests of individual
73 Board members.

74 **Q. Has the change in ownership as a result of the acquisition impacted customers and**
75 **operations?**

76 A. The change in ownership at the Pennichuck Corporation level has been transparent to
77 both customers and operations. Management changes at the senior executive level have
78 not affected customer services or operations. Mr. Ware will address this issue in more
79 detail.

80 **Rate Case**

81 **Q. Why is the Company filing a rate case at this time?**

82 A. The Settlement Agreement requires the regulated companies owned by Pennichuck
83 Corporation to file full rate cases simultaneously by no later than June 1, 2013.

84 **Q. Please discuss the ratemaking structure utilized in this filing.**

85 A. The rate making structure utilized in this filing is set forth in the Settlement Agreement.
86 There are two elements to the structure. The first element provides for recovery of the
87 City Bond Fixed Revenue Requirement ("CBFRR"). The second element is akin to
88 traditional ratemaking and provides for recovery of operating expenses and equity. Mr.
89 Goodhue and Mr. Ware will provide more detailed information relative to the structure.

90 **Q. How was the CBFRR amount determined?**

91 A. The CBFRR amount was determined in accordance with the Settlement Agreement.
92 Under the approved formula, the CBFRR amount is based on the pro-rata share of the
93 City's Acquisition Debt obligation, which is calculated based on the Company's

94 percentage share to the total share of the three regulated utilities. Mr. Goodhue will
95 provide more detail as to the computation of the CBFRR amount in his testimony.

96 **Q. How was the Company's allowable rate of return determined?**

97 A. The Company utilized the formula agreed to in the Settlement Agreement. The formula
98 applies a cost of equity based on the average of interest rates on 30-year Treasury bonds
99 for the most recent 12 months plus 3.0 percentage points. Mr. Goodhue will provide
100 more detail in his testimony.

101 **Q. In your testimony in DW 11-026, you testified that the savings related to the**
102 **acquisition of Pennichuck Corporation by the City of Nashua would result in**
103 **operational savings of \$1.7 million. Were the savings achieved?**

104 A. Yes. As described in Mr. Goodhue's testimony, the anticipated savings of \$1.7 million
105 were achieved by reducing public company costs in Pennichuck Corporation and
106 eliminating certain executive management positions in Pennichuck Water Works, Inc.

107 **Compliance with Settlement Agreement**

108 **Q. The Settlement Agreement provided for the establishment of a rate stabilization**
109 **fund by Pennichuck Water Works. Has the fund been established?**

110 A. Yes. The City Acquisition Debt included \$5 million for the establishment of a rate
111 stabilization fund by Pennichuck Water Works, Inc. The \$5 million was contributed by
112 Pennichuck Corporation to Pennichuck Water Works, Inc. upon completion of the
113 acquisition. The PWW Rate Stabilization fund has been maintained in accordance with
114 the procedures set forth in the Settlement Agreement in DW 11-026. Mr. Goodhue will
115 discuss the rate stabilization fund in more detail in his testimony.

116 **Q. Has the MARA been recorded on the Company books and how was the MARA**
117 **treated for ratemaking purposes?**

118 A. As agreed to in the Settlement Agreement, the MARA was computed and recorded on
119 the books at the time of the City's acquisition of Pennichuck. The MARA was
120 removed from the traditional ratemaking process because it is only recoverable as part
121 of the CBFRR.

122 **Q. Did the Company declare and provide dividends or distributions to its parent,**
123 **Pennichuck Corporation?**

124 A. Yes. The Commission approved the payment of dividend and distributions from paid in
125 capital to the parent corporation, Pennichuck Corporation, for the purpose of enabling
126 the City to satisfy the City's obligations for the City Acquisition Bonds. On February
127 22, 2013, Pennichuck East Utility, Inc. recorded the following distribution of its parent
128 Pennichuck Corporation: a dividend in the amount of \$71,787 (from retained earnings)
129 and a distribution from paid in capital of \$752,171. The distribution reflected the
130 Company's share of the funding of the City acquisition debt for 2012.

131 **Q. Did the Company make any payments to the City in 2012 for its Eminent Domain**
132 **costs?**

133 A. The Company did not make any payments to the City in 2012 pursuant to Paragraph
134 III. D. 4. of the Settlement Agreement. As part of the discovery process in the rate
135 cases, it may be advisable for the parties to discuss the mechanism by which the
136 Commission will audit the final Eminent Domain Amount.

137
138 **Temporary Rates**

139 **Q. Will the Company be seeking a temporary rate increase?**

140 A. Under the terms of the Settlement Agreement, the Company is required to seek
141 temporary rates in accordance with RSA 378:27.

142 **Communications**

143 **Q. Please describe Pennichuck's efforts to communicate with the City of Nashua,**
144 **other affected communities, and customers relative to the rate filing?**

145 A. We have been communicating with Nashua and other communities with customers
146 relative to rate information and the rate case process for some time. These constituents
147 have been notified of the filing of the Notices of Intent to File Rate Schedules and the
148 estimated rate increase. We will continue to keep them informed as the rate cases
149 proceed. We have indicated to the communities that our staff is available to meet with
150 each community as it desires. Customers will also be informed directly in accordance
151 with Puc 1203.02.

152 **Conclusion**

153 **Q. How do the rates requested compare to the rates that would have been required**
154 **had Pennichuck Corporation remained a publicly traded company?**

155 A. The requested increase in rates consists of a permanent rate increase of 9.97% and a
156 step increase of 2.25%. The combined rate increase is 12.21%. Under the prior
157 ownership structure, the requested increase, including the step increase, would have
158 approximated 21.98% as shown in Exhibit JLP-2. The higher rate assumes that the
159 public company cost savings and the savings associated with the management
160 restructuring are not achieved. The higher rate also assumes an overall rate of return of
161 5.96% on a higher rate basis. The annual impact on the average single family customer
162 would have been to increase monthly cost to \$11.52 versus the \$6.40 per month

163 requested in the filing as shown in Exhibit JLP-3. I believe these results demonstrate
164 the sound judgment of the City of Nashua in pursuing the acquisition of Pennichuck
165 Corporation.

166 Q. Does this complete your testimony?

167 A. Yes.