

NORTHERN UTILITIES, INC.

TESTIMONY OF

DAVID L. CHONG

IN SUPPORT OF ISSUANCE OF UP TO \$50,000,000 IN LONG-TERM DEBT

New Hampshire Public Utilities Commission  
Docket No. DG 14-\_\_\_\_

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

2 A. My name is David L. Chong. My business address is 6 Liberty Lane West, Hampton,  
3 New Hampshire, 03842.

4 **Q. By whom are you employed and in what capacity?**

5 A. I am Director of Finance and Assistant Treasurer for Unitil Service Corp., a service  
6 company subsidiary of Unitil Corporation that provides managerial, financial, regulatory  
7 and engineering services to Unitil Corporation's utility subsidiaries. I am also the  
8 Assistant Treasurer of Northern Utilities, Inc. ("the Company" or "Northern Utilities")  
9 and Unitil Corporation's other utility subsidiaries. My responsibilities are primarily in  
10 the areas of financial planning and analyses, treasury operations and banking  
11 relationships.

12 **Q. Please summarize your professional and educational background.**

13 A. I have approximately thirteen years of professional experience in the energy and utilities  
14 industries. From 2001 through 2005, I worked for Exxon Mobil Corporation in various  
15 facilities engineering roles with my last position as a Senior Project Engineer. From  
16 2005 through 2008, I worked for RBC Capital Markets Corporation in the energy  
17 investment banking group, where I provided corporate finance and mergers and  
18 acquisitions advisory services. While at RBC, I raised equity and debt capital on  
19 numerous occasions for various energy companies. I also advised on several buy-side  
20 and sell-side mergers and acquisitions transactions. From 2008 through 2009, I worked  
21 for El Paso Exploration & Production Company in its business development group as an  
22 Acquisition & Divestiture Principal. I began working for Unitil Service in August 2009

1 as the Director of Finance. I hold a Master's Degree in Business Administration from  
2 Tulane University and a Bachelor of Science degree in Mechanical Engineering with  
3 Honors from the University of Texas at Austin.

4 **Q. Have you previously testified before the Commission or other regulatory agencies?**

5 A. Yes, I have previously presented testimony before this Commission in Dockets DE 09-  
6 236, DG 09-239, DE 10-028, DG 11-069 and DG 13-086. I have also testified before the  
7 Maine Public Utilities Commission and Massachusetts Department of Public Utilities on  
8 several occasions on various financial, ratemaking and regulation matters.

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

10 A. The purpose of my testimony is to explain and support the Company's F-4 petition  
11 requesting authorization to issue to institutional investor(s) senior notes evidencing  
12 unsecured long-term debt in an aggregate amount of up to \$50,000,000 (hereinafter  
13 referred to as the "Notes"). The Company is filing at the same time an identical petition  
14 for authorization to issues securities with the Maine Public Utilities Commission.

15 **Q. What is the Company specifically requesting at this time?**

16 A. Northern Utilities is seeking the Commission's approval to issue an aggregate principal  
17 amount of up to \$50,000,000 of Notes. The Notes will be sold at par and will have mixed  
18 maturities and bear a fixed coupon of not more than 6.5%.

19 **Q. When did the Company complete its last long-term debt financing?**

20 A. Northern Utilities completed its last long-term debt financing in March 2010 when it  
21 issued \$25,000,000 of 5.29% senior notes due March 2020. This financing was approved  
22 by the Commission by Order No. 25,068 in Docket DG 09-239, issued on January 22,

1 2010. The Company currently has two other tranches of debt outstanding including  
2 \$30,000,000 of 6.95% senior notes due December 2018 and \$50,000,000 of 7.72% senior  
3 notes due December 2038. See, Order No. 24,905, Docket DG 08-079, issued October  
4 10, 2008.

5 **Q. What capital improvements have been made to the Company's distribution system**  
6 **since the last financing in March 2010?**

7 A. The Company has spent \$114 million on distribution system capital expenditures from  
8 March 2010 through December 31, 2013 in New Hampshire and Maine combined. A  
9 summary of this spending by major category is included in Schedule DLC-1.

10 **Q. How does the Company finance its capital expenditures?**

11 A. The funding to meet capital expenditures is derived primarily from internally generated  
12 funds, which consist of net cash flows from operating activities. Northern Utilities  
13 supplements internally generated funds, as needed, through short-term borrowings under  
14 the Unitil Corporation Cash Pool, which is supported by bank borrowings under Unitil  
15 Corporation's credit facility.

16 **Q. Please describe the key terms of the proposed long-term debt financing.**

17 A. Northern Utilities is targeting to issue, at par, to institutional investors unsecured senior  
18 notes in an aggregate amount of \$40,000,000. The Notes are expected to be issued under  
19 similar terms and provisions of the Note Purchase Agreements of the existing senior note  
20 tranches. The Company is targeting a mix of long-term maturities of 10-year and 30-year  
21 issuances. A mix of 10-year and 30-year securities allows for the Company to match the  
22 long-lived nature of its utility assets with the long-term average life of the securities

1 while achieving an attractive and market-based overall weighted yield. Furthermore, an  
2 issuance of mixed maturities ensures that the Company is not exposed to refinancing risk  
3 at a single point in time, and instead provides for the ability to access the market at  
4 multiple times to diversify its financing risk. The Company will work closely with its  
5 Placement Agent, Merrill, Lynch, Pierce, Fenner & Smith Incorporated (the “Placement  
6 Agent”), to determine the ultimate size of the offering, maturities, coupon and other terms  
7 based on market conditions and investor interest at the time of pricing.

8 **Q. Why is the Company requesting in its petition to issue up to \$50,000,000 if the**  
9 **Company is targeting an offering of \$40,000,000?**

10 A. The Company would like to reserve flexibility in the size of the offering to facilitate the  
11 marketing process. The Company anticipates several investors in this offering process.  
12 In the event the Company receives competitively priced bids exceeding \$40,000,000, the  
13 Company believes it may be beneficial to accommodate the investors up to a maximum  
14 offering size of \$50,000,000. For example, a scenario could include two investors that  
15 offer favorable pricing on bid indications of \$20,000,000 and \$25,000,000, respectively.  
16 Instead of reducing the allocations to the investors, and risk losing the favorable pricing  
17 terms, the Company would like to have the flexibility to accommodate the investors’ bids  
18 up to a maximum total offering size of \$50,000,000. For pro forma purposes, I have  
19 shown the effect of the maximum total offering size of \$50,000,000 throughout the  
20 remainder of my testimony.

1 **Q. What do you expect the Company's indicative credit rating to be for the offering?**

2 A. Unitil and its utility subsidiaries do not have a public credit rating. The Company's  
3 current outstanding senior notes have a private rating of NAIC-2(-) by the National  
4 Association of Insurance Commissioners (NAIC) which is the regulatory agency of the  
5 Company's existing insurance investors. An NAIC-2(-) rating is generally considered in  
6 the financial community to be equivalent to the BBB- investment grade range of ratings  
7 by Standard and Poor's rating agency. Unitil's Placement Agent plans to market this  
8 offering as an NAIC-2(-) investment grade credit.

9 **Q. What are the current indicative coupon rates for this Notes offering?**

10 A. If issued today, the indicative coupon rate for a 10-year maturity is estimated to be  
11 approximately 4.20%-4.45%, and the rate for a 30-year maturity is estimated to be  
12 approximately 5.26%-5.51%. The estimated coupon rate for the 10-year maturity was  
13 derived by applying a projected credit spread of 150-175 basis points to the US Treasury  
14 benchmark rate (as of March 26, 2014) of 2.70%. Similarly, the estimated coupon rate  
15 for the 30-year maturity was derived by applying a projected credit spread of 170-195  
16 basis points to the US Treasury benchmark (as of March 26, 2014) rate of 3.56%. The  
17 expected credit spread is based on the Company's discussions with the Placement Agent  
18 and relies upon the Placement Agent's market expertise and review of recent comparable  
19 utility transactions.

1 **Q. How does the indicative coupon rate for this offering compare to the last offering in**  
2 **March 2010?**

3 A. The last offering in March 2010 was also marketed as an NAIC-2 credit. The credit  
4 spread at that time was 190 basis points. The ten-year U.S. Treasury benchmark rate was  
5 3.39% resulting in a total coupon rate of 5.29% for a ten-year maturity. Thus, the credit  
6 spread of a 10-year maturity is currently expected to be slightly lower than the last  
7 offering, and the U.S. Treasury yields are down as a result of governmental monetary and  
8 fiscal support, resulting in a lower anticipated overall coupon rate for a 10-year maturity  
9 for this upcoming offering.

10 **Q. Why is Northern Utilities proposing a 6.5% maximum coupon rate in its petition?**

11 A. Market conditions can rapidly change, and Northern Utilities does not anticipate pricing  
12 until May 2014. In addition, while the Placement Agent anticipates the above credit  
13 spreads, there can be no assurance that the Company achieves this result. Therefore,  
14 Northern Utilities is requesting approximately 100 basis points on top of the anticipated  
15 indicative coupon rate of 5.26%-5.51% of the 30-year maturity to provide for flexibility  
16 in the credit spread and maturities, and in the event treasury yields widen from the date of  
17 this petition and to pricing. As explained later, the Company will submit an update to the  
18 Commission of the final coupon rate once the Notes have been priced.

1 **Q. How does the current US treasury yield benchmark compare to yields in prior**  
2 **market periods?**

3 B. From a longer term perspective, treasury yields are near historically low levels. Credit  
4 spreads have tightened since the Company’s last offering, and NAIC-2 all-in coupon  
5 rates are near historic lows and continue to be attractive.

6 **Q. How does Northern Utilities intend to use the net proceeds of the issuance of the**  
7 **Notes?**

8 A. The Company intends to utilize the proceeds of the Notes financing as follows: (1) to  
9 repay outstanding short-term indebtedness incurred for additions, extensions and  
10 betterments to the Company’s property, plant and equipment such as the Company’s cast  
11 iron and bare steel replacement programs in both jurisdictions; and (2) to defray the costs  
12 and expense of the financing or for other lawful general corporate purposes.

**NORTHERN UTILITIES, INC.**  
**SOURCES AND USES OF FUNDS**  
**Proposed Sale of \$50,000,000 Senior Unsecured Notes**  
*(\$ In Thousands)*

<b><u>Sources of Funds</u></b>	
Proposed Sale of Senior Unsecured Notes	\$50,000
<b>Total Sources of Funds</b>	<b><u>\$50,000</u></b>
<b><u>Uses of Funds</u></b>	
Repay Short-Term Debt and General Corporate Purposes	\$49,495
Fees and Expenses	505
<b>Total Uses of Funds</b>	<b><u>\$50,000</u></b>



1 **Q. What other benefits will the Company use the proceeds of this Notes offering for?**

2 A. The Notes offering will help to position the Company's balance sheet to pursue its  
3 significant capital investment plans as outlined in the Company's testimony in the current  
4 base rate case proceeding in New Hampshire (DG 13-086), and the recently completed  
5 base rate case proceeding in Maine (2013-00133). The Company's capital budget for  
6 2014 is included in Schedule DLC-1.

7 **Q. How will the Notes offering affect the capital structure, including short-term debt of**  
8 **the Company?**

9 A. The Company's actual and pro forma capital structure is shown below. On a total  
10 leverage basis, including short-term debt, the Company's debt-to-capitalization ratio will  
11 remain at approximately 55%-56% on an actual and pro forma basis, since the net  
12 proceeds of the offering will be used to repay short-term debt. With the reduction in  
13 short-term debt, the Company will have the benefit of having a stronger balance sheet to  
14 finance its ongoing capital construction program. Although I have not included any pro  
15 forma adjustments to Common Equity in the table below, the Company expects its equity  
16 capitalization will continue to grow in the future as well through retained earnings,  
17 providing for a lower debt-to-capitalization ratio and balanced overall capitalization.

**NORTHERN UTILITIES, INC.**  
**CAPITAL STRUCTURE AS OF DECEMBER 31, 2013**  
**Proformed for the Issuance and Sale of \$50,000,000 Senior Unsecured Notes**  
*(\$ In Millions)*

	<u>Actual</u>	<u>Adjustments</u>	<u>Pro Forma</u>
	<u>12/31/13</u>	<u>12/31/13</u>	<u>12/31/13</u>
Senior Unsecured Notes	\$105.0	\$50.0	\$155.0
Common Equity	119.4	0.0	119.4
<b>Long-Term Capitalization</b>	<b>\$224.4</b>	<b>\$50.0</b>	<b>\$274.4</b>
Short-Term Debt	43.0	(43.0)	0.0
<b>Total Capitalization</b>	<b>\$267.4</b>	<b>\$7.0</b>	<b>\$274.4</b>
<b>Total Debt / Total Capitalization</b>	<b>55.3%</b>		<b>56.5%</b>

1 **Q. How will the Notes offering affect the Company's weighted cost of long-term debt?**

2 A. The Company's weighted cost of long-term debt is currently 6.92% which reflects the  
 3 weighted cost of the Company's existing tranches of debt discussed previously. This  
 4 offering, at a maximum coupon rate of 6.50%, will lower the Company's weighted cost  
 5 of long-term debt. The Company anticipates that this will benefit ratepayers in its next  
 6 base rate case proceeding.

7 **Q. What are the projected issuance costs for the proposed Notes offering?**

8 A. Under the terms of the engagement letter with the Placement Agent, Northern Utilities  
 9 will pay a placement fee of 0.80% of the principal amount of the Notes at the time of  
 10 closing. Additionally, the Company will be responsible for legal expenses, including all  
 11 fees and expenses of both the Company's and investor's counsel incurred in commencing  
 12 the offering and sale of the Notes. The Company has estimated total legal costs of  
 13 \$100,000 for this transaction, including legal services for corporate financing and  
 14 regulatory services as well as the cost for investor's counsel. Northern Utilities also  
 15 estimates \$5,000 for miscellaneous expenses including potential out-of-pockets expenses

1 for the Placement Agent under the terms of the engagement letter. The current estimate  
2 is that the total costs associated with the issuance of the Notes will be about \$505,000.

3 **Q. What types of investors participate in the private placement process?**

4 A. Typically, the investors for this type of transaction will be insurance companies that have  
5 a demand for longer term maturity securities and have a strong familiarity with the utility  
6 sector. The Placement Agent has recommended a strategy to market the Notes to a select  
7 handful of existing and prospective private placement investors that are active  
8 participants in the utility sector, are familiar with the Company's business and operations,  
9 and that have demand for long-term securities. The Placement Agent has a strong market  
10 presence within the utility sector and has recommended this marketing strategy as the  
11 most appropriate for three reasons. First, this strategy recognizes the importance of the  
12 Company's existing relationship with current investors and gives them an opportunity to  
13 participate in a new issuance. Second, the Placement Agent is actively marketing deals  
14 within the utility sector and therefore knows which external investors are the most likely  
15 to show strong interest and make competitive offers. Third, the Placement Agent has  
16 indicated that given the size of the issuance of up to \$50,000,000, a competitive market  
17 can best be established with the above strategy. The Placement Agent expects this  
18 strategy will yield competitive offer(s) indicative of current utility NAIC-2 market  
19 conditions. The Placement Agent also anticipates that some investors will opt to not  
20 make a bid once they realize they may not be competitive on the price guidance provided  
21 by the Placement Agent during the marketing period.

1 Q. **Does Northern Utilities expect the Private Placement Market to be receptive to this**  
2 **offering?**

3 A. Yes. Northern Utilities believes that the private placement market will be receptive to  
4 this offering, similar to the previous deal completed by the Company in March 2010,  
5 where the Company was viewed favorably by the private placement market. According  
6 to the Placement Agent, investors have been attracted by the Company's growth and  
7 performance in its sector and strong management team, and will welcome the opportunity  
8 to invest further in Northern Utilities. In addition, the regulated nature of distribution  
9 utilities generally are targeted investment alternatives for some investors.

10 Q. **What is the timetable for the proposed Notes offering?**

11 A. The Company expects to market the Notes offering in early May 2014. Once the offering  
12 is priced, the Company will submit an update to the Commission with the final pricing  
13 parameters including coupon rate. The Company expects investors will allow a 90-day  
14 period after pricing to close the transaction. This would place closing of the offering in  
15 early August 2014. While this timetable is currently the Company's best estimate, it is  
16 possible that due to unforeseen market or other conditions, the timing may be adjusted.

17 Based on this timeline, Northern Utilities is requesting an Order from the Commission  
18 approving the Notes offering on or before June 30, 2014. This will provide for the  
19 necessary expiration of the appeal period prior to the final closing expected in early  
20 August 2014.

21 Q. **Does this conclude your testimony?**

22 A. Yes, it does.