

STATE OF NEW HAMPSHIRE

Inter-Department Communication

DATE: August 28, 2018

AT (OFFICE): NHPUC

FROM: Stephen P. Frink ^{SAF}
Director, Gas & Water Division

NHPUC 28AUG18AM11:30

SUBJECT: DG 18-103 Northern Utilities, Inc.
Proposed Franchise Expansion in Kingston and Atkinson

TO: Commissioners
Docket File
Service List

Staff Recommendation – Gas & Water Division

Staff recommends the petition be granted by order for the following reasons:

- 1) Northern Utilities, Inc. (Northern or Company) stated, and has demonstrated through its New Hampshire natural gas operations, that it has the requisite financial, engineering and managerial capability to operate the proposed service territory;
- 2) Northern provides service to adjacent towns and already provides service to a discrete portion of Atkinson;
- 3) Results of the Discounted Cash Flow (DCF) analysis, using conservative revenue estimates, indicate that proposed expansion will benefit existing customers through lower rates;
- 4) An anchor customer, a customer with significant energy usage, exists in each of the towns and will be making a significant contribution towards the construction of the main extension and has contracted for service to commence immediately upon completion of the project, or shortly thereafter;
- 5) In addition to the anchor customers, other consumers along the new line and in the expanded franchise territory will have access to natural gas as an alternative to more expensive fuel;
- 6) The Kingston and Atkinson Selectmen have filed letters of support for the proposed expansion;
- 7) Expansion of the service territory will not adversely affect existing gas supply resources.

Staff further recommends that the Commission forego a hearing on the merits and issue an order approving Northern's petition at its earliest convenience to allow Northern to commence construction as soon as possible. The reasons for issuing an order as soon as possible and without a hearing are as follows:

- 1) The New Hampshire Department of Transportation (DOT) plans to pave some of the roads on the proposed route of the main extension and once the DOT paving is completed there

will be a (5) year construction moratorium on that section of the route. Issuing an order expeditiously will enable Northern to complete the project prior to DOT paving.

- 2) Lewis Builders Development, Inc. (Lewis Builders), the anchor customer for the proposed Atkinson expansion, has requested service by December 1, 2018.
- 3) An order of notice was issued, a prehearing conference held, and comments supporting the proposed franchise expansions filed. No comments have been filed opposing the proposed expansions.

Background and Analysis

On July 3, 2018, Northern, filed with the New Hampshire Public Utilities Commission (Commission) a petition for approval of authority to operate in the Towns of Kingston and Atkinson. The petition includes a letter of support from the Kingston Board of Selectmen. On August 2, 2018 the Town of Atkinson Selectmen filed a letter stating that the initial response from residents indicates the proposed project will be met with great enthusiasm.

On July 11, 2018, the Commission issued an order of notice scheduling a prehearing conference and technical session for July 24, 2018, which were held as scheduled. The OCA filed a letter of participation in the docket pursuant to RSA 363:28. No other parties filed motions to intervene.

On July 31, 2018, Staff filed a letter stating that the parties were not requesting adoption of a procedural schedule as Staff had commenced discovery and the parties agreed to proceed with discovery on an informal basis, Staff intended to file a recommendation regarding the franchise request before the end of August and that the parties would meet to determine whether they support the Staff recommendation and would communicate their separate recommendations to the Commission.

Staff issued three sets of discovery, including one prior the July 24, 2018, technical session. At the technical session Staff, Northern and the OCA discussed Northern's business and engineering plans related to the proposed expansion. Staff has reviewed the filing, data responses and spoken with officers of the Lewis Builders regarding its properties (Atkinson Country Club) and development plans.

Findings

Financial Analysis

Northern used an appropriate economic analysis to determine the cost and benefit to serve each of the towns and justify the proposed expansions, demonstrating that the incremental system investment required to provide utility service to the new franchise areas will be borne by the customers to be served and not subsidized by existing customers.

Northern conducted a DCF analysis to evaluate the economic feasibility for each of the two proposed line extensions, the financial analysis is required under Northern's tariff applicable to

Northern Line Extension Policy and is a methodology that the Commission has found to be the appropriate framework to evaluate the financial viability of the large system expansions.¹

Northern's DCF analysis compares the estimated distribution revenues to estimated costs related to the proposed expansion, including the incremental costs associated with the main and service extensions, operations and maintenance expense, depreciation expense and property and other taxes. These amounts are reflected on an annual basis and result in the annual after-tax cash flow associated with the proposed line extension. The annual cash flows are then discounted over ten years to a present value at Northern's after-tax weighted cost of capital to determine the Net Present Value (NPV) of the project. If the NPV is negative, the new customer(s) must pay the negative amount as a Contribution in aid of Construction (CIAC).

Northern does not include Allowance for Funds Used During Construction (AFUDC) as a cost in its economic analysis, although AFUDC is applied for accounting purposes. For short-term projects the Company's AFUDC formula uses its short-term borrowing, resulting in minimal AFUDC costs for smaller projects. Northern does not include the AFUDC cost in its DCF analysis as the cost is minimal. Staff agrees that excluding AFUDC cost in this instance is appropriate as the AFUDC cost would be *de minimis*, given the short construction period and low interest rate.

Kingston Expansion

The results of the financial analysis justify the proposed Kingston expansion.

Northern currently serves the Town of Plaistow and will be extending an existing main located in Plaistow 1.4 miles to serve the Benevento Bituminous LLC (Benevento) asphalt plant located in Kingston. There are thirty two (32) commercial and fourteen (14) residential prospective customers along the main extension.

The DCF analysis of the proposed line extension to serve Benevento produces a zero NPV over ten years based on a conservative revenue estimate, actual returns over that period should be positive, and if the analysis were extended over the life of the project (average service life of mains and services) the NPV would be significantly higher. Benevento has requested service by April 1, 2019.

The revenue analysis only includes distribution revenue from Benevento over ten years based on its actual prior fuel usage, actual revenue from the line extension should be well in excess of that used in the analysis as Northern has reviewed the assessor's data on the prospective customers along the Kingston main extension and estimates that over the next five years 60% of the commercial buildings and 40% of the residential building will convert to natural gas. Benevento is making a significant CIAC and has entered into a service agreement with Northern and based on those commitments it is reasonable to assume the Benevento asphalt plant will be in operation well beyond 10 years. Likewise, premises where businesses and residents have converted to natural gas can be expected to continue natural gas service indefinitely.

¹ See Order 22,297 issued August 28, 1996, approving Northern firm gas transportation agreement and expansion of services.

Northern has provided a map of the proposed line extension route and described each of the construction phases in detail. The route, construction plans and cost estimates appear reasonable. The route is designed to serve the anchor customer and cost estimates are based on the design specifications using average stock room pricing for materials and contract unit prices for outside labor.

Benevento Contract for Installation of Gas Service

Benevento entered into a contract for the installation of gas service on June 13, 2018 and signed an addendum to the contract on July 18, 2018.

The contract sets the CIAC to be paid by Benevento and includes customer covenants with respect to the amount of gas to be used. The customer covenants include a warranty from Benevento that the asphalt plant will use natural gas for a defined period of time and sets minimum annual usage amounts that, if not met, allows Northern to recalculate the CIAC requirement and bill Benevento for a CIAC deficiency if one exists. The warranty, in addition to the CIAC to be paid in advance of construction, serves to ensure that existing customers will not subsidize customers along the new main extension.

Atkinson Expansion

The results of the financial analysis justify the proposed Atkinson expansion.

The DCF analysis of the proposed line extension to serve the Atkinson Country Club and Condominium development produces a positive NPV over ten years based on a conservative revenue estimate, actual returns are likely to be higher, and if the analysis were extended over the life of the project (average service life of mains and services) the NPV would be significantly higher. Lewis Builders has requested service by December 1, 2018.

Northern currently serves a discrete section of the Atkinson and will be extending an existing main 3.8 miles to serve the Atkinson Country Club and condominium development, and thereafter install on site another 0.4 miles of main and ten service lines. In addition to the Atkinson Country Club, there are eight (8) commercial and one hundred and twenty nine (129) residential prospective customers along the main extension.

The revenue analysis only includes distribution revenue from the Atkinson Country Club and phase one of the condominium development over ten years based on the actual prior Atkinson Country Club fuel usage and projected fuel use for phase one of the condominium development. Actual revenue from the line extension should be well in excess of that used in the analysis. Phase one of the Lewis Builders development plans is the construction of 288 units and later phases include construction of over 600 more condominiums, a hotel and an entertainment complex. Lewis Builders will be performing the excavation and backfill required to install the proposed mains and services to serve the planned development. To accomplish that Lewis Builders is committing significant resources that would otherwise have added approximately \$1.7 million to the project cost, if Northern were to perform the work. In addition to the future

load/revenue growth expected from further Lewis Builders development, it is reasonable to expect Northern will realize additional load/revenue from adding a number of the 137 potential customers located along the proposed main extension. Premises where businesses and residents have converted to natural gas can be expected to continue natural gas service indefinitely.

Northern has provided a map of the proposed line extension route and described each of the construction phases in detail. The route, construction plans and cost estimates appear reasonable. The route is designed to serve the anchor customer and cost estimates are based on the design specifications using average stock room pricing for materials and contract unit prices for outside labor.

Northern Service to Customers Outside of Approved Franchise Territory

Currently, Northern is serving customers outside of its approved franchise territory, customers located in the Town of Atkinson. In DE 88-096 Northern petitioned for Commission approval to serve a discrete area of Atkinson, which was granted by Order 19,147 issued August 22, 1988. Lewis Builders filed a letter in support of a Northern request to serve an additional area of town. The letter was filed in advance of that main installation to that additional area.

Although the issue has been raised and identified in the immediate docket (Staff Recommendation prepared by Randy Knepper, Director of Safety & Security), it does not need to be addressed in this docket. Approving the proposed expansions will resolve the issue of Northern serving Atkinson customers that are outside of its currently approved franchise area, but the proposed franchise expansion in the immediate docket stands on its own merits and is in the public interest.

Support of Towns along Proposed Main Extension

Both the Kingston and Atkinson Boards of Selectmen filed a letter of support with the Commission strongly supporting Northern's request to extend natural gas service in their community, stating that the extension would have a positive impact on the community.

Expanded Access to Natural Gas

Expanding service to Kingston and Atkinson will enable two new large customers to lower energy costs by converting to natural gas and to fuel future development. It will also make it more economical for businesses and residences along the proposed main extensions to convert.

No Adverse Effect on Supply Resources

Other than two anchor customers that have requested and committed to taking service, Northern does not have definitive plans to provide service to any specific, new customers on the proposed line extensions at this time. The expected combined capacity requirements of the forecasted load along the two proposed line extensions is approximately 0.2 percent of Northern's overall capacity requirement.

Benevento is expected to be a firm, summer only, transportation customer and as such will not be purchasing natural gas from Northern and will have very little impact on Northern's supply resources. Additional sales or transportation customers that are added along the extension should not have an adverse effect on supply resources, as Northern's current supply capacity is sufficient to meet the potential growth along the new line extensions.

SERVICE LIST - EMAIL ADDRESSES - DOCKET RELATED

Pursuant to N.H. Admin Rule Puc 203.11 (a) (1): Serve an electronic copy on each person identified on the service list.

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FILING INSTRUCTIONS:

- a) Pursuant to N.H. Admin Rule Puc 203.02 (a), with the exception of Discovery, file 7 copies, as well as an electronic copy, of all documents including cover letter with:
- DEBRA A HOWLAND
EXECUTIVE DIRECTOR
NHPUC
21 S. FRUIT ST, SUITE 10
CONCORD NH 03301-2429
- b) Serve an electronic copy with each person identified on the Commission's service list and with the Office of Consumer Advocate.
- c) Serve a written copy on each person on the service list not able to receive electronic mail.