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THE STATE OF NEW HAMPSHIRE



PUBLIC UTILITIES COMMISSION
21 S. Fruit Street, Suite 10
Concord, N.H. 03301-2429

TDD Access: Relay NH
1-800-735-2964

Tel. (603) 271-2431

FAX (603) 271-3878

Website:
www.puc.nh.gov

NHPUC 4 JAN 19 PM 3:14

January 4, 2019

Debra A. Howland, Executive Director
New Hampshire Public Utilities Commission
21 South Fruit Street, Suite 10
Concord, New Hampshire 03301-2429

Re: DW 18-174: Pennichuck East Utility, Inc. ("PEU" or "Company")
Interim Petition for Approval of 2018 Qualified Capital Project Adjustment Charge
("QCPAC") Budget
Staff Recommendation for Approval

Dear Ms. Howland:

On November 18, 2018, PEU filed an Interim Petition for Approval of its 2018 QCPAC budget in accordance with Commission Order No. 26,179 (October 4, 2018) in Docket DW 17-128. Specifically, PEU's Interim QCPAC Petition requests that the Commission, 1) approve PEU's proposed 2018 projects for recovery under the QCPAC mechanism in 2019, subject to the Commission's audit and prudence review of the final costs associated with those projects; 2) receive PEU's proposed 2019 and 2020 projects for informational purposes only; and 3) take such further action and make such other findings and orders as in its judgement may be just, reasonable, and in the public good. The purpose of this letter is to recommend that the Commission grant approval of the Company's proposed 2018 budget for recovery under the QCPAC mechanism in 2019 as well as accept PEU's proposed 2019 and 2020 budgets for informational purposes only. Following is a detailed explanation relative to Staff's review and recommendation for approval of PEU's Interim QCPAC Petition.

Summary of QCPAC Mechanism

In Order No. 26,179, the Commission approved a Settlement Agreement which not only provided for a general rate increase for PEU but also established a revised ratemaking structure for the Company. This new ratemaking structure is similar to that which was approved by the Commission in Order No. 26,070 (November 7, 2017) for PEU's affiliate, Pennichuck Water

Works, Inc. (“PWW”), in DW 16-806. Like PWW, PEU’s approved ratemaking structure was principally necessitated by the City of Nashua’s (“City”) acquisition of PEU in 2012.¹ Among the impacts of this acquisition was the elimination of PEU’s access to equity markets for obtaining financing capital. As a result, the Company is now primarily reliant upon debt financing to meet its capitalization needs. PEU’s new ratemaking structure is designed with the goal of enabling the Company to have the necessary cash flows to adequately satisfy its debt service and loan covenant requirements.

In order to promote the Company’s ability to maintain adequate cash flows, PEU’s QCPAC mechanism enables the Company to receive rate recovery on essentially all of its debt financed capital projects undertaken and completed between rate proceedings. Order No. 26,179 established the following criteria which PEU’s proposed QCPAC projects must meet in order to be eligible for rate recovery: 1) the projects proposed by PEU must be completed, in service, and used and useful within the previous fiscal year for which the QCPAC filing is made; 2) the capital projects must have been financed by debt that has been approved by the Commission in accordance with RSA 369; and 3) the capital projects must specifically correspond with a capital budget which has been previously submitted and updated by PEU and approved by the Commission.

PEU’s annual QCPAC filings, which are anticipated to be received by approximately February of each year, consist of two parts. The first part will contain a detailed reporting on the prior fiscal year’s eligible QCPAC projects previously approved by the Commission, including the actual amounts expended to acquire and/or construct such assets. That information will be subject to review and audit by Staff and will be the basis for the annual QCPAC rate approved by the Commission. The QCPAC rate will be based on 1) 1.1 times the debt service associated with the approved and completed Qualified Capital Project’s (“QCP’s”), and 2) the incremental property taxes applicable to the approved and completed QCP’s. The second part shall contain 1) a proposed budget for all capital project expenditures planned during the fiscal year in which the QCPAC filing is made for the purpose of receiving preliminary approval from the Commission; and 2) a forecast of capital project expenditures for the following two fiscal years, for informational purposes only. It is anticipated that the Commission’s rulings concerning PEU’s annual QCPAC requests will occur by approximately October of each year.

For purposes of the initial establishment of PEU’s QCPAC rate mechanism, Order No. 26,179 required the Company to file an Interim QCPAC Petition within forty-five days of the issuance of that order. The purpose of the filing was to enable PEU to request and receive approval from the Commission for its fiscal year 2018 QCPAC budget as well as submit its projected capital expenditures for fiscal years 2019 and 2020. Upon approval of its 2018

¹ See *Joint Petition of City of Nashua, et.al*, Order No. 25,292 (November 23, 2011) in Docket DW 11-026.

QCPAC budget, PEU will submit its first full QCPAC filing in February of 2019, including a formal request for the establishment of an initial QCPAC rate based on the completed and in-service QCP's related to the Company's previously approved 2018 QCPAC budget.

PEU's Interim QCPAC Filing

In support of its Petition in the instant docket, PEU included the Direct Testimony of Donald L. Ware, the Company's Chief Operating Officer. On December 4, 2018, a Letter of Participation was submitted by the Office of the Consumer Advocate ("OCA") in accordance with RSA 363:28. There are no other intervenors in this docket.

Pursuant to Order No. 26,179, PEU's Interim QCPAC Petition includes a proposed budget of its 2018 QCP's for Commission approval as well as a forecast of its anticipated capital project expenditures for the years 2019 and 2020, for informational purposes. The submissions for all three years are based on the Capital Expenditure (Capex) budgets which were approved by PEU's Board of Directors in January of 2018. PEU's Board approved capital budgets for 2018-2020 were as follows: 2018 - \$4,826,000; 2019 - \$1,233,000; 2020 - \$3,542,000. For purposes of PEU's Interim QCPAC filing, however, while its projected capital expenditures for 2019 and 2020 remain unchanged, the Company's anticipated 2018 capital expenditures are now projected to be \$5,181,688; an increase of approximately \$356,000.

Mr. Ware's testimony explains that PEU's projected 2018 budget consists of the following:

- **PWW – PEU Interconnection: \$3,889,775**

The necessity of this project was explained in two prior PEU dockets: DW 17-055 and DW 17-071. Essentially, in order to meet an anticipated increase in future demand, PEU entered into a special wholesale water supply contract with PWW.² In that contract, PEU agreed to pay the costs associated with an interconnection with PWW in order to receive the necessary water supply under the contract. The cost of the interconnection is largely financed by a \$2.4 million State Revolving Fund ("SRF") loan from the NH Department of Environmental Services ("NHDES").³ The project was also approved for a \$600,000 grant from the NHDES Drinking Water and Groundwater Trust Fund ("DWGTF").

² See Commission Order No. 26,049 dated August 23, 2017.

³ See Commission Order No. 26,006 dated April 19, 2017.

- **Brady Avenue Main Replacement: \$598,000**
This project involves the replacement of approximately 2,400 linear feet of substandard water main with 8" ductile piping in the Town of Derry. The majority of the project will be financed by a \$570,000 SRF loan.⁴
- **Hillcrest Road Main Replacement: \$240,000**
This project encompasses the replacement of 1,200 linear feet of failing 12" thin wall ductile iron main located in the Town of Litchfield with new high density polyethylene pipe. The majority of this project will be financed by an SRF loan originally approved in the amount of \$245,000.⁵ However, PEU currently anticipates SRF funding for this project in the amount of \$235,125.
- **Miscellaneous Projects: \$453,913**
The remaining projects included in PEU's projected budget for 2018 consist largely of routine annual maintenance capital projects including meter replacements, pump replacements, service replacements and installations, etc. These projects, as well as portions of the three projects previously discussed, will be financed by an estimated \$1,376,563 long-term loan from CoBank, ACB. PEU anticipates submitting a filing for approval of this financing with the Commission in early 2019.

Mr. Ware's testimony states that based on the 2018 QCP's proposed in the instant filing, PEU anticipates that it will be requesting an approximate 3.43 percent surcharge in its initial full 2019 QCPAC filing in order to recover additional revenues of \$284,131. If approved, this would increase the monthly billings of an average PEU residential customer by \$2.59.

Staff's Review and Recommendation

Staff reviewed PEU's filing and propounded discovery on December 6, 2018. The Company submitted its responses to Staff's discovery on December 13, 2018. Additionally, a report dated January 4, 2019 from Utility Engineer, Joseph Vercellotti, has been attached to this correspondence. Mr. Vercellotti's report pertains to the engineering and operational aspects of PEU's filing and focuses mainly on the proposed projects for 2018. In his report, Mr. Vercellotti indicates that the majority of the 2018 projects proposed by PEU are being financed by loans and grants administered by the NH Department of Environmental Services (NHDES). As such, these projects received financing approval based, in part, on a prudence review by NHDES. Further, with regard to the remaining 2018 projects proposed by PEU that are not financed by NHDES administered programs, Mr. Vercellotti states that these projects are related to routine annual maintenance and are necessary to ensure safe and reliable service. Therefore, Mr. Vercellotti

⁴ See Commission Order No. 26,006 dated April 19, 2017.

⁵ See Commission Order No. 26,006 dated April 19, 2017.

DW 17-179: Pennichuck Water Works, Inc.
Staff Recommendation for Approval of Interim QCPAC Petition
January 4, 2019

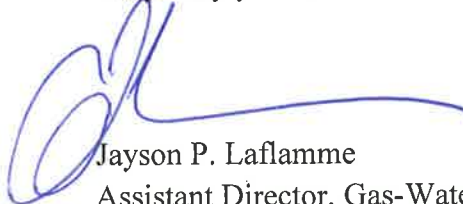
concludes that the Company's proposed 2018-2020 projects appear to be prudent. A copy of Mr. Vercellotti's report is attached to this correspondence.

Based on its review of PEU's filing, Staff recommends that the Commission approve the proposed 2018 QCPAC budget in the amount of \$5,181,688 for recovery under the QCPAC mechanism which is to be filed by PEU in February of 2019 and will be subject to the Commission's audit and prudence review of the final costs associated with the budgeted projects. Staff also recommends that the Commission accept submission of PEU's proposed 2019 capital projects budget of \$1,233,000 and 2020 capital projects budget of \$3,542,000, for informational purposes only.

Prior to filing this letter with the Commission, Staff provided a final draft to the OCA. The OCA, however, provided no comment with regard to Staff's recommendations.

Thank you for your assistance with this matter. If you have any questions relative to this filing, please do not hesitate to contact me.

Very truly yours,

A handwritten signature in blue ink, appearing to read 'J. Laflamme', with a long horizontal flourish extending to the right.

Jayson P. Laflamme
Assistant Director, Gas-Water Division

Attachments: 01/04/19 Report of Joseph Vercellotti, Staff Engineer

cc: Service List

STATE OF NEW HAMPSHIRE

Inter-Department Communication

DATE: January 4, 2019
AT (OFFICE): NHPUC

FROM: Joseph M. Vercellotti, P.E. *JMV*
Utility Engineer

SUBJECT: Pennichuck East Utility, Inc. (PEU)
DW 18-174 Qualified Capital Project Adjustment Charge (QCPAC)

TO: Steve Frink, Director Gas-Water Division, NHPUC
Jayson Laflamme, Asst. Director Gas-Water Division, NHPUC

Introduction

On November 18, 2018, PEU filed an Interim Petition for Approval of its 2018 QCPAC budget in accordance with Commission Order No. 26,179 (October 4, 2018) in Docket DW 17-128. Specifically, PEU's Interim QCPAC Petition requests that the Commission, 1) approve PEU's proposed 2018 projects for recovery under the QCPAC mechanism in 2019, subject to the Commission's audit and prudence review of the final costs associated with those projects; 2) receive PEU's proposed 2019 and 2020 projects for informational purposes only; and 3) take such further action and make such other findings and orders as in its judgement may be just, reasonable, and in the public good.

This review pertains to the assessment of the engineering and operational aspects of the proposed. The purpose of this memo is to recommend that the Commission grant approval of the Company's proposed 2018 budget for recovery under the QCPAC mechanism in 2019 as well as accept PEU's proposed 2019 and 2020 budgets for informational purposes only.

Staff recommends Commission approval of the proposed projects to be financed through programs administered by the New Hampshire Department of Environmental Service (NHDES).

RSA 486:14 established the State Water Pollution Control and Drinking Water Revolving Funds to be administered by NHDES. Applicants are required to submit detailed construction plans for NHDES review and approval, with prudence being one of the criteria for approval per NHDES rule:

Env-Dw 1102.31 "Planning" for purposes of an eligible infrastructure project means evaluating alternative solutions to drinking water system problems, selecting the most cost-effective alternative through a systematic screening procedure, and developing an asset maintenance and renewal plan or asset management program.

NHDES also provides funding through state grants per NHDES rule:

Env-Dw 1001.01 Purpose. The purpose of these rules is to implement RSA 486-A, which provides for state grants to: (a) Public water systems that have been required to comply with the surface water treatment rules of the federal Safe Drinking Water Act of 1986 and Env-Dw 716; (b) Public water systems which interconnect to form regional water systems; and (c) Public water systems which investigate the groundwater contributing area of wells with recorded levels of chemical contaminants, excluding methyl tertiary-butyl ether (MTBE).

Projects funded through state grants are for the public good and a very limited impact on rates, as assets funded through grants are treated as a contributions-in-aid-of-construction for rate making purposes and therefore do not increase rate base.

Staff also recommends approval of the proposed projects that are not being funded through NHDES administered programs, as those projects are related to routine annual maintenance and necessary to ensure safe and reliable service.

Following is a summary of the projects and Staff's review and recommendation for approval of PEU's Interim QCPAC Petition.

Proposed 2018 Projects

PEU's projected 2018 QCPAC budget consists of the following projects:

- **Pennichuck Water Works, Inc. (PWW) – PEU Interconnection: \$3,889,775**
The necessity of this project was explained in two prior PEU dockets: DW 17-055 and DW 17-071. Essentially, in order to meet an anticipated increase in future demand, PEU entered into a special wholesale water supply contract with PWW. In that contract, PEU agreed to pay the costs associated with an interconnection with PWW in order to receive the necessary water supply under the contract. The cost of the interconnection is largely financed by a \$2.4 million State Revolving Fund ("SRF") loan from NHDES. The project was also approved for a \$600,000 grant from the NHDES Drinking Water and Groundwater Trust Fund ("DWGTF").
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originally approved in the amount of \$245,000. However, PEU currently anticipates SRF funding for this project in the amount of \$235,125.

- **Miscellaneous Projects: \$453,913**

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These projects, as well as portions of the three projects previously discussed, will be financed by an estimated \$1,376,563 long-term loan from CoBank, ACB. PEU anticipates submitting a filing for approval of this financing with the Commission in early 2019.

PEU indicated that if the 2018 QCP's proposed in the instant filing are approved by the Commission, that PEU will be requesting an estimated 3.43 percent surcharge in its initial full 2019 QCPAC in order to recover additional revenues of \$284,131. This will increase the monthly billings of an average PEU residential customer by \$2.59.

Conclusion

Based on the assessment of the engineering and operational aspects of the proposed 2018 water projects described in the petition, testimony, and data requests, PEU's proposed 2018 to 2020 projects and estimated costs appear to be prudent and as such, I support approval of the company's petition. Please let me know if you need anything further in this regard.

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.

Executive.Director@puc.nh.gov
amanda.noonan@puc.nh.gov
Christopher.tuomala@puc.nh.gov
donald.kreis@oca.nh.gov
james.brennan@oca.nh.gov
jayson.laflamme@puc.nh.gov
ocalitigation@oca.nh.gov
rwh@rathlaw.com
steve.frink@puc.nh.gov

Docket #: 18-174-1 Printed: January 04, 2019

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.**