# TAB 9

**Testimony of Larry Goodhue and Attachments**

**STATE OF NEW HAMPSHIRE**

**BEFORE THE**

**PUBLIC UTILITIES COMMISSION**

Docket No. DW 20-153

Pittsfield Aqueduct Company, Inc.
Permanent Rate Proceeding

**DIRECT TESTIMONY OF LARRY D. GOODHUE**

November 13, 2020

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## I. INTRODUCTION

**Q. Would you please state your name, address and position with Pittsfield Aqueduct Company, Inc.?**

**A.** My name is Larry D. Goodhue. My business address is 25 Walnut Street, Nashua, New Hampshire. I am the Chief Executive Officer and Chief Financial Officer of Pittsfield Aqueduct Company, Inc. (the "Company" or "PAC"). I have been employed with the Company since December 2006. I am also the Chief Executive Officer and Chief Financial Officer of Pennichuck Corporation ("Pennichuck"), which is the corporate parent of PAC.

**Q. Please describe your educational background.**

**A.** I have a bachelor's in science degree in Business Administration with a major in Accounting from Merrimack College in North Andover, Massachusetts. I am a licensed Certified Public Accountant in New Hampshire; my license is currently in an inactive status.

**Q. Please describe your professional background.**

**A.** Prior to joining Pennichuck, I was the Vice President of Finance and Administration and previously the Controller with METRObility Optical Systems, Inc. from September 2000 to June 2006. In my more recent role with METRObility, I was responsible for all financial, accounting, treasury and administration functions for a manufacturer of optical networking hardware and software. Prior to joining METRObility, I held various senior management and accounting positions with several private and publicly-traded companies.

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

**A.** As Chief Executive Officer, I am responsible for the overall management of Pennichuck and its subsidiaries, including PAC, and I report to the Board of Directors. I work with the Chief Operating Officer, the Corporate Controller, Treasurer, Assistant Treasurer, Director of Water Supply, Chief Engineer, Distribution Manager, the Director of Human Resources and the Director of Information Technology to: (1) implement short and long-term financial and operating strategies, (2) insure the adequate funding of debt and expenses, and (3) enable Pennichuck's utility subsidiaries to provide high quality water service at affordable rates, on a consistent basis.

**Q. Have you previously testified before this or any other regulatory commission or governmental authority?**

**A.** Yes. I have submitted written testimony in the following dockets before the New Hampshire Public Utilities Commission (the "Commission"):

- Financings for PEU – DW 12-349, DW 13-017, DW 13-125, DW 14-020, DW 14-191, DW 14-282, DW 14-321, DW 15-044, DW 16-234, DW 17-055, DW 17-157, DW 18-132, DW 19-069 and DW 20-081;
- Financings for Pittsfield Aqueduct Company ("PAC") – DW 15-045 and DW 16-235;
- Financings for Pennichuck Water Works, Inc. ("PWW") – DW 14-021, DW 14-130, DW 15-046, DW 15-196, DW 16-236, DW 17-183, DW 19-026, DW 20-055, DW 20-064 and DW 20-157.

- Permanent and Temporary Rate Increase Proceedings for: PWW – DW 13-130, DW 16-806 and DW 19-084; PEU – DW 13-126 and DW 17-128; and PAC – DW 13-128.

## II. PURPOSE OF THIS TESTIMONY

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

**A.** The purpose of my testimony is to provide information supporting PAC's request for temporary rate relief, permanent rate schedules, and request to modify PAC's ratemaking structure, including: (1) relevant historical information regarding the City of Nashua's acquisition of Pennichuck in early 2012; (2) information concerning how the ratemaking structure set forth in the Settlement Agreement approved by this Commission in Order No. 25,292 in Docket No. DW 11-026 has been operating since the 2012 acquisition; (3) information concerning PWW recent settlement modifying its ratemaking structure in Docket No. DW 16-806 and Docket No. DW 19-084, as well as for PEU in Docket No. DW 17-128, should be applied to PAC; and (4) information supporting the rate relief requested by PAC and the specific modifications to PAC's current ratemaking structure demonstrating that such requests are just, reasonable and in the public interest.

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

**A.** The other witness in this case, who is also providing written testimony in this proceeding, is Chief Operating Officer Donald Ware. This individual holds this role for both PAC and Pennichuck, as well as the other subsidiaries of Pennichuck. His testimony will describe his qualifications, history and previous instances of testimony before the Commission.

## III. HISTORY AND IMPLICATIONS OF THE CITY OF NASHUA ACQUISITION

**Q. Mr. Goodhue, before explaining the details of the proposed financings, would you please provide some history regarding the ownership of PAC and how that history supports PAC's request for approval of permanent and temporary rate relief?**

**A.** PAC as a corporate entity is wholly-owned by Pennichuck, which is, in turn, is a closely-held private corporation that is wholly-owned by the City of Nashua, New Hampshire, as its sole shareholder. The City of Nashua acquired its ownership of Pennichuck on January 25, 2012, pursuant to this Commission's Order No. 25,292 (23, 2011) (Approving Acquisition and Settlement Agreement). Prior to this acquisition by the City of Nashua, Pennichuck's shares were traded on the NASDAQ public stock exchange. For purposes of my testimony, I refer to the period prior to the City's acquisition as "pre-acquisition" and the period after as "post-acquisition."

**Q. Did the City's acquisition affect the way in which PAC operates as a utility?**

**A.** Yes. The change in the ultimate ownership of PAC's parent, Pennichuck, from a publicly-traded investor-owned utility to ownership by the City has had important consequences for the operation of PAC. These same issues were involved with PAC's regulated sister companies, PWW and PEU which are also wholly owned by Pennichuck. As such, my testimony in PWW's recent rate cases, Docket No. DW 16-806 and Docket No. DW 19-084, as well as PEU's recent rate case in Docket No. DW 17-128, applies equally or substantially to this case. In light of the settlement regarding PWW's ratemaking methodology, I will be referring to PWW's rate cases in DW 16-806 and DW 19-084, or PEU's rate case under DW 17-128, throughout my testimony.

**Q. What are the important similarities in the way the City's acquisition affected the operation of PAC and PWW or PEU?**

**A.** One of the most important consequences is that PAC, PWW, or PEU, after the City's acquisition of Pennichuck, no longer have access to the private equity markets as a method of financing a portion of their capital needs. Companies that have access to the private equity markets, or Investor Owned Utilities ("IOU's"), where a 50/50 debt/equity ratio is considered optimal, but at an elevated cost to rate payers due to a return on equity needed to benefit public company shareholders, in the form of share value and appreciation and/or the regular and consistent payment of dividends to their shareholders.

As such, and as contemplated during the Commission's proceeding to approve the City's acquisition of Pennichuck in DW 11-026, after the acquisition, PAC, PWW, and PEU are expected to finance their on-going capital needs entirely and solely through the issuance of debt.

**Q. Does reliance solely on debt to finance PAC's operations have impacts on PAC's customers?**

**A.** Yes. As contemplated during the acquisition proceedings, one positive result of this anticipated debt financing is that the weighted cost of PAC's capital structure is significantly lower than it was prior to the City's acquisition, due to the elimination of the public company ROE dynamic discussed previously. As for PAC, this ROE existed at 9.75% post-tax pre-acquisition (approximately 16% pre-tax at Corporate tax rates in existence at that time, and approximately 12% pre-tax at current Corporate tax rates).

This lower cost of capital has had and will continue to have direct beneficial benefits for PAC's customers.

**Q. Does reliance solely on debt to finance PAC's operations have consequences for PAC's rate setting methods and procedures?**

**A.** Yes. As also contemplated in the acquisition Docket DW 11-026, the City's acquisition of Pennichuck and the resulting need to finance utility operations solely with debt has required modifications to PAC's (and Pennichuck's other utilities') ratemaking methods and procedures. As a result of this reliance on debt, PAC is much more dependent on the direct relationship of cash flow generated from rates, as it relates to the ongoing repayment of debt in support of ongoing capital investments. Under the previous ownership structure, the allowed return on public company equity allowed for extra cash generated to cover the repayment of debt obligations, as well as adequate coverage of operating expenses and dividend obligations to shareholders. This is even more important for PAC than it is for PWW or PEU, as both PWW and PEU have access to external debt financing for their capital project needs based upon the size of their financial operating levels, and the magnitude of their capital project needs. PAC, on the other hand, has no access to external debt funding except State Revolving Fund ("SRF") or Drinking Water and Groundwater Trust Fund ("DWGTF") loans for certain eligible projects, which may qualify from time to time. This causes an even greater reliance upon PAC's overall rate structure, in support of fully funding cash flow and working capital needs, in order to remain financially viable long term. While PAC has the ability to access funds from Pennichuck, as a part of the consolidated group, utilizing Pennichuck's Working Capital Line of Credit as a backstop for periodic and temporary or seasonal cash flow needs, its rates must produce sufficient cash to repay those borrowings, as Pennichuck is obligated by its lender to completely "clean out" and pay that facility down to $0 for at least 30 consecutive days in each calendar year.

**Q. What is your opinion of the Company's specific business risk profile in comparison with the overall water utility industry?**

A. There are a number of Company specific factors that need to be considered in evaluating its business risk profile relative to the entire water utility industry. The first factor is the Company's small size. Small size magnifies the impact of certain unavoidable fixed costs, such as: state and local property taxes; and, property & casualty insurance. Another factor magnifying the Company's business risk is its geographically small single-state service territory. Water companies that operate in multiple states across larger geographic areas are generally considered to have less business risk as they are less reliant on a single regulator or on the weather in a specific geography.

**Q. Please explain financial risk and why that is important to the Company in meeting its long-term obligations.**

A. Financial risk reflects the assessment of the Company's corporate financing policies and practices including, but not necessarily limited to: liquidity (i.e., credit lines), and debt capitalization and the ability to raise sufficient debt to finance necessary capital expenditures, in relation to the Company's operating and capital spending plans. More specifically, financial risk considers and seeks to measure the Company's ability to finance its capital additions program while meeting its debt obligations on a timely and consistent basis. Ratings agencies such as Moody's Investor Service, Standard & Poors, and others have developed a number of key ratios (credit benchmarks) which quantify financial risk by business risk category. Other things being equal, the higher the business risk the higher the credit benchmarks necessary to achieve an overall favorable credit rating. Certain aspects of the components of the Company's current rate structure, as defined under the Settlement Agreement for Docket No. DW 11-026, helps to mitigate some of this financial risk, including the establishment of the City Bond Fixed Revenue Requirement ("CBFRR") and the overall Rate Stabilization Fund ("RSF") funds from that Order, as defined later in this testimony.

**Q. Does the Company have a bond credit rating for its debt?**

A. No. The Company does not currently have a bond credit rating designated for its debt, as a stand-alone company. However, the Company completed discussions about the potential refinancing of its existing intercompany notes payable with a banking institution in 2013, and as a part of that process, the banking institution did an evaluation of the credit worthiness of PAC. This lender declined to offer replacement financing for PAC, for these intercompany notes, based upon the risk factors, and the business risk factors spoken about previously in this testimony.

**Q. What factors support the Company's creditworthiness?**

A. In discussions with potential lenders, PAC's credit risk rating does have certain favorable elements in existence, including: stability & predictability of the regulatory environment, cost and investment recovery (ability and timeliness), operational efficiency, scale of capital program and asset condition, overall organization structure, and its funding from operations compared to its debt position.

**Q. With respect to the Company's creditworthiness, what challenges face the Company?**

A. The Company faces several challenges, including: the Company's capital additions program; the need to properly maintain a program of ongoing infrastructure replacement; the need for adequate rate relief to maintain financial ratios and service existing and new debt; and, the small size of the Company.

**Q. What are the primary factors needed to maintain an acceptable credit profile?**

A. Certain elements of the Company's current rate structure, as provided for in DW 11-026, are important in giving PAC access to necessary low cost debt funding, needed to maintain its operations without any major disruptions, and to maintain compliance with potential financial covenants (as discussed earlier in this testimony). These elements include the CBFRR, the RSF, the inclusion of the Municipal Acquisition Regulatory Asset ("MARA") as an element of Generally Accepted Accounting Principles ("GAAP") basis equity, the prescribed formulaic approach to the allowed return on common equity (as discussed above), and the current corporate governance structure of Pennichuck and PAC.

It is important to note, however, that the RSF established in DW 11-026, only gave PAC access to those funds at PWW through intercompany borrowings, but did not provide for any basis of repayment of borrowed funds from the RSF (back to PWW), or the specific bifurcation of RSF funds exclusively for the usage by PAC. This is due in part to the fact that PAC's current rate structure does not include an element that includes the Company's ability to repay intercompany debt obligations to Pennichuck or PWW, as an element of its allowed revenues.

To address this problem, in DW 16-806, the bifurcation and reservation of specific RSF funds for PAC was approved. In this docket, we are seeking approval to accept those funds into PAC's rate structure, a modified rate structure for the further bifurcation of those funds to backup the three proposed buckets of allowed revenues (CBFRR, OERR, and DSRR), as was established for PWW in DW 16-806 and PEU in DW 17-128. We are also including intercompany debt obligations in the computation of the DSRR portion of allowed revenues, such that the Company's rate structure provides for the cash resources to service and repay those obligations.

**Q. Why is an acceptable credit profile important to the Company, and what is being done in this case to provide for that?**

A. An acceptable credit profile is important in that it allows the Company to continue to have access to debt funding, from its available sources. Even though the SRF and DWGTF programs do not include financial covenants like other commercial loan programs, if the Company is deemed not to be financially viable, even those funds will not be available to them for capital project investments. Additionally, as the Company's only other source of debt funding currently is intercompany borrowings from Pennichuck, it must maintain a level of financial viability that is accretive to the overall financial health of the corporate group, or access to those funds could be jeopardized. The implementation of the modified rate structures being sought in this case, as approved for PWW in Dockets No. DW 16-806 and DW 19-084, and PEU in Docket No. DW 17-128, are essential to provide PAC with a rate structure that is needed to provide for long term financial viability and an acceptable credit profile, as well as rate stability for its customers over the long term. This is not only important for PAC, but also important in its intercompany obligations to Pennichuck and

PWW, as PAC's ability to properly pay for intercompany usage of the resources provided from Pennichuck and PWW is vital to the overall credit worthiness of both Pennichuck and PWW, in their ability to comply with debt covenants, and maintain a credit rating that is accretive to the entire corporation group, which is beneficial to PAC and its customers. The overall impact of the modified ratemaking methodology being sought in this case, on the credit profile of the companies can be further explained by referring to supplemental testimony provided in DW 19-084 on August 21, 2019, and further clarification as submitted on October 9, 2019.

## IV. RATEMAKING METHODOLOGY SETTLEMENT IN PWW'S RATE CASE, DOCKET NO. DW 16-806 AND DW 19-084, AND PEU'S RATE CASE, DOCKET NO. DW 17-128

**Q. Mr. Goodhue, you noted the impacts of the City's acquisition of Pennichuck on its subsidiaries, PAC, PEU, and PWW, were similar. Please provide an overview of the relevant issues from PWW's 2016 and 2019 rate case, as well as PEU's 2017 rate case.**

**A.** In PWW's Docket DW 16-806 and DW 19-084, as well as PEU's Docket DW 17-128, we were faced with many of the same issues that presently face PAC. The City's acquisition resolved almost a decade of intense disputes between the City and the pre-acquisition management of Pennichuck, and was premised on the assumption that the City's ownership of the utilities would produce consistently lower rates for ratepayers over time, as compared to the previous investor-owned utility structure. On July 19, 2017, the parties to Docket No. DW 16-806 filed a Settlement Agreement, which was approved by the Commission, which substantively updated the ratemaking methodology for PWW as adopted in Docket DW 11-026. Likewise, on July 18, 2018, the parties to Docket No. DW 17-128 filed a Settlement Agreement which substantially updated the ratemaking methodology for PEU as adopted in DW 11-026, and in conformity with the updated ratemaking methodology for PWW put in place in Docket No. DW 16-806. The Commission also approved this settlement. Additionally, on June 24, 2020, the parties to Docket No. DW 19-084 filed a Settlement Agreement which further updated the ratemaking methodology for PWW as adopted in Docket DW 11-026 and modified in Docket No. DW 16-806. This settlement was approved by the Commission. As is outlined in the DW 16-806 Settlement Agreement, Pennichuck's experiences since the DW 11-026 ratemaking methodology was approved demonstrated some deficiencies in that methodology, but our experience also provided a basis to understand what improvements to the methodology were needed. Those improvements are reflected in the DW 16-806 Settlement Agreement. The DW 16-806 Settlement Agreement is attached as Exhibit LDG-1 (excluding exhibits). The Settlement Agreement for the more recent revisions agreed to in DW 19-084 is attached as Exhibit LDG-2. The settlement contains a flow chart at pages 63-69 that is helpful in visualizing the ultimate goal of the changes to PAC's ratemaking structure.

**Q. What are the primary benefits of the modified rate structures approved under the DW 16-806, DW 17-128, and DW 19-084 Settlement Agreements, as it pertains to PAC?**

**A.** The modifications to PAC's ratemaking structure will increase PAC's ability to provide for adequate cash flows to repay its debts, and will provide lenders with the confidence in PAC's ability to repay its debt obligations, all of which is fundamental for PAC to be able to continue to access needed debt for infrastructure replacement and operations. This is especially important for PAC, with its inherent limitations to access of external debt financing, as addressed earlier in this testimony. As such, their ability to meet their cash flow needs is vitally important in the Company's ability to repay any SRF or DWGTF loan obligations and/or the repayment of intercompany loan obligations to Pennichuck, as its only other source of internal debt financing, which is dependent upon the corporation as a whole being able to meet its debt and covenant compliance obligations, all of which are dependent upon rates that provide for an adequacy of bottom line profitability and cash flow liquidity.

**Q. Did the Parties to the DW 16-806 Settlement Agreement anticipate that the modified rate structure would also apply to PAC?**

**A.** Yes. The Settlement Agreement specifically includes the following provision on pages 14-15:

> "*The Settling Parties agree that the current $5,000,000 Rate Stabilization Fund (RSF) maintained by PWW, which was established under the Original Rate Structure, should be re-allocated amongst the three Penn Corp utilities such that PWW's allocated share of the RSF shall now be $3,920,000, with the remaining balance of $1,080,000 to be allocated between PEU and PAC. The allocation to PWW is based on the respective three utilities' last Commission approved revenue requirements as detailed on* Exhibit 6 *of this Settlement Agreement. The Settling Parties agree that the $1,080,000 portion of the RSF that is proposed to be allocated between PEU and PAC shall remain in PWW's RSF cash account until such time that rate case filings are made for PEU and PAC. At that time, the modified rate structure for PWW that is proposed in this settlement agreement will also be requested as the proposed rate structures for both PEU and PAC. If the respective rate structures for PEU and PAC are approved by the Commission, the $1,080,000 will then be transferred from PWW's RSF funds to the respective RSF funds to be established in PEU and PAC.*"

It is important to note that included in the Settlement Agreement and subsequent Order affirming that Agreement in Docket No. DW 17-128 for PEU, that the $980,000 referenced above for funds to be transferred to PEU, was affirmed and put in place subsequent to that Order's issuance. The $100,000 reserved for PAC remains at PWW awaiting an approval for a transfer of those RSF funds to PAC, as a part of this proceeding.

**Q. Is PAC now seeking to implement the same ratemaking structure described in the 16-806 Settlement Agreement, as well as the further modifications approved for PWW in 19-084?**

**A.** Yes. This is the ideal time for the new ratemaking structure to apply to PAC. PAC currently has a need to fully cover its cash flow obligations and provide for overall covenant compliancy within the corporate group. This is especially important, as under its existing rate structure, given the fact that PAC's depreciation lives are well in excess of its debt instrument lives, giving rise to the fact that the cash flow generated from depreciation does not fully meet the principal repayments on issued debt, either to outside lenders such as the SRF or DWGTF, or as a repayment of funds on intercompany loans used to fund de minis and ongoing "run rate" capital expenditures for PAC. This is especially important in the upcoming year or more, as the New Hampshire Department of Environmental Services ("NHDES") has worked with the Company on a required need to bring certain capital projects to bear, which will provide for a safety net for water supply to the system in the Town of Pittsfield. Currently that infrastructure contains a single water main that runs down Catamount Road on the northern side of the PAC water system, into the downtown area where the distribution system exists. Should a failure occur on that line, the entire system would be out of water, which would be extremely problematic for a number of reasons. The Company did attempt to install a duplicate main down Catamount Road, but the NHDOT rejected the installation. In the alternative, within the next several years, the NHDES is seeking to have PAC install a water tank on the southern side of the Suncook Highway to provide for storage and supply, should a main break occur on the single watermain located on Catamount Road. Given this individual circumstance, it places even more importance on the need to secure a modified rate structure for PAC, which will fully support the cash flows of the Company, giving it the ability to fund its ongoing operating costs, as well the service of its external debt payments, including the anticipated SRF or DWGTF loan for this new tank.

Additionally, as PAC has no current access to the RSF funds through PWW because it has no approved ability to repay any monies borrowed from those funds, the new ratemaking methodology is needed to: (1) insure adequate EBITDA coverage for PAC, as it relates to covenant requirements for itself or the corporate group as a whole; (2) provide adequate cash flows from revenues to pay debt service, CBFRR and operating expenses; and (3) provide adequate support funds in the form of the RSF accounts, to provide for cash funding during times of revenue shortfalls and expense growth above inflationary levels between rate case filings.

**Q. Of the $1,080,000 of RSF funds to be transferred from PWW to PEU and PAC, how much is reserved for PAC, and please explain whether that amount is insufficient to fully fund those RSF accounts and how does the Company anticipate handling the full funding of those accounts.**

**A.** Of the $1,080,000 in RSF funds available from transfer from PWW to PEU and PAC, $980,000 is reserved for PEU and $100,000 for PAC. As delineated in Mr. Ware's testimony in support of this filing, the calculated need to fully fund the new RSF accounts is $186,000. As such, the available transferrable cash funds are $86,000 short of the overall assessed need at this time. This shortfall is anticipated to be funded in one of the following ways: (1) if the Material Operating Expense Factor ("MOEF") is approved as a rate structure element in this case, then the Company will only seek funding of the RSF accounts to the imprest level of $100,000 at this time, or (2) if the MOEF is not approved in this case, then it will seek full funding to the $186,000 imprest level by refilling the RSF funds to their required levels over the next three years via a deferred debit included as an element of the allowed revenues in this case.

## V. OVERVIEW OF REQUESTS FOR RATE RELIEF AND MODIFICATIONS TO PAC'S RATEMAKING STRUCTURE

**Q. Mr. Goodhue, before describing the details of the proposed request for permanent rate relief, could you provide an overview of the nature of the proposal?**

**A.** The proposed rate relief proposal consists of two principal components. First, as set forth in our full rate filing materials which are described in more detail by Mr. Ware in his testimony, PAC is requesting an increase in annual revenues of approximately $86,783, or 11.18%. The second, component of PAC's requested relief is its request, as I described above and as is set forth in PAC's Petition for Further Modifications in Ratemaking Structure, for approval of the modified ratemaking methodology as was applied to PWW in Docket No. DW 16-806 and Docket No. DW 19-084. Adopting the

DW 16-806 and DW 19-084 modified ratemaking methodologies would allow PAC to provide adequate cash flow to cover its overall cost of operations, including prudent operating expenses and debt service costs, and provide its debt lenders with reasonable expectations of future rates that are directly related in a common sense way to PAC's long-term, post-acquisition capital requirements which rely on entirely on debt. To restate this, essentially these modifications expressly acknowledge that PAC's reliance on debt financing requires a ratemaking method that is based on a fixed multiple of the annual debt service on existing debt, with the balance of the allowed revenue requirement tied to coverage of prudent, normal and ongoing operating expenses.

**Q. Mr. Goodhue, in practical terms, what would be the impact on the average residential monthly bill if all aspects of PAC's proposed rate relief were approved by the Commission?**

**A.** Overall, the average single family residential monthly bill is currently \$58.12. Our requested rate increase would increase the average base amount in a customer's bill by approximately \$6.50 per month, bringing the average monthly bill to \$64.62.

## VI. <u>SUMMARY OF PROPOSED RATE RELIEF AND IDENTIFICATION OF PROPOSED MODIFICATIONS TO PAC'S RATEMAKING STRUCTURE</u>

**Q. Mr. Goodhue, would you please briefly describe the rate relief requested in this proceeding by PAC?**

**A.** As is summarized above, with the filing of its full rate case documents as required by the Commission's administrative rules, PAC is requesting the Commission to approve, pursuant to its general permanent rate-setting authority, a rate increase of 11.18%, bringing its allowed revenues to a projected level of $862,927, as detailed in PAC's rate case filing at Tabs 12 and 13.

**Q. Is PAC requesting a step increase in this proceeding?**

**A.** No. PAC is not requesting a step increase in this proceeding. It is, however, filing for temporary rates at current rates. A filing and testimony requesting this has been prepared and is being filed contemporaneously with the filing of all other documents to this proceeding.

**Q. Is the rate increase the only relief that PAC is seeking in this proceeding?**

**A.** No. For the background reasons explained earlier in this testimony, PAC is also requesting that the Commission approve, pursuant to its general ratemaking authority, such modifications to the ratemaking methodology for PAC that it approved for PWW in DW 16-806 and DW 19-084, and as adopted by PEU as approved in DW 17-128. Please see PAC's Petition for Further Modifications to Ratemaking Structure at Tab 11. As described below, in order to provide a clear factual basis for the Commission's review of the proposed modifications, PAC has prepared its ratemaking schedules to reflect not only the operation of the current ratemaking method as established by the Commission in DW 11-026, but also operation of the modifications requested by PAC in its petition under the methodology approved in DW 16-806 and DW 19-084. The rate increase being requested by PAC in this case is based on the DW 16-806 and DW 19-084 modified methods reflected in the ratemaking schedules.

**Q. Would you briefly describe the basis for this requested rate relief in more detail?**

**A.** The fundamental basis for this request is that it represents the revenues required to cover PAC's current operating expenses and to meet the demonstrated costs of servicing PAC's direct debt obligations plus its share of the CBFRR. PAC has prepared its ratemaking schedules to demonstrate this fundamental basis. This overall rate increase also included the implementation of the modified rate structure elements approved for PWW in DW 16-806 and DW 19-084, and PEU in DW 17-128, exclusive of the QCPAC program. These include:

- An OERR revenue component of allowed revenues, in its elemental pieces of an MOERR, and NOERR and an MOEF, with the associated MOERR RSF fund;
- A DSRR-1.0 revenue component of allowed revenues, along with the associated DSRR RSF fund;
- A DSRR 0.1 revenue component of allowed revenues;
- A five-year average test period to replace a single test year;
- Actual NH Business Enterprise Tax cash payments to be included in the OERR portion of allowed revenues;
- Prioritization of the usage of the DSRR 0.1 funds;
- The recovery and inclusion of SFR and DWGTF debt issuance costs in the Company's allowed revenues; and
- The re-establishment of imprest levels of RSF accounts, as a reconciliation mechanism.

**Q. Please describe how the five-year averaging PAC is requesting in this proceeding works under the modified rate methodology.**

**A.** The purpose of the five-year averaging is to develop pro forma test year data regarding revenues and expenses which is less likely to reflect unusual or abnormal events, such as a uniquely dry or wet summer. Under the DW 16-806 modified rate methodology, the "test year" revenues use the trailing five-year average consumption at the most recently approved volumetric rates and fixed charges. The five-year trailing average consumption determination shall be based on the four calendar years immediately preceding the designated test year for which the rate case is filed as well as the test year itself. Additionally, all direct test year expenses which are affected by differences in consumption, including but not limited to purchased water expense, electricity expense, and chemical treatment expense, also include pro forma adjustments to reflect the pro forma difference in consumption between the five-year average and the test year. Although the modified methodology includes this five-year average test period for computing its revenue deficiency, the prior Settlement Agreements that recommended this five-year average specifically states that neither Staff nor the OCA are precluded from making an alternative recommendation in place of the five-year average with respect to the determination of revenue deficiency.

**Q. Please describe how you are asking the five-year average be implemented for PAC.**

**A.** We plan to calculate the full effect of the five-year average for the 2019 test year under this rate case and include that pro forma calculation into this filing.

**Q. Please explain why PAC needs rate relief at this time?**

A. First, PAC has invested approximately $409,000 in capital improvements and infrastructure replacements since its last filed rate case for test year 2012 under Docket No. DW 13-128, and the current rates do not include the necessary dollars in the existing revenue requirement to fund the repayment of those debt instruments, for both principal and interest. Second, operating expenses of the Company have increased at or above the rate of inflation, as well as increases in property taxes, since that last filed permanent rate filing. In the case of property taxes, the Company does proactively process abatements for valuations that are deemed to be in excess of allowed or reasonable levels, given the current RSA allowing for the taxation of Utility Property as Real Property at both the State and Local level. Since its last rate case, PAC successfully negotiated a settlement for property taxes with the Town of Pittsfield, for which the results of that settlement is included in the operating expenses included in the filing schedules in support of the requested revenue increase herein. Overall, the rate case being pursued at this time is necessary to provide for the ongoing cash flow needs to fund ongoing operating expenses and fund the repayment of debt obligations, as available to PAC in support of its ongoing obligations to its ratepayers.

## VII. RATEMAKING SCHEDULES ARE FORMATTED PURSUANT TO PAC'S CURRENT AND PROPOSED RATEMAKING METHDOLOGY

**Q. Please discuss the format of the ratemaking schedules filed by PAC upon which the requested rate relief is based.**

**A.** PAC's requested rate relief is based on the modified ratemaking structure set forth in its filed ratemaking schedules. As further described in the testimony of Mr. Ware, these schedules embody financial information and resulting rates attributable to three distinct scenarios: (1) application of the modified ratemaking structure approved by this Commission in DW 11-026; (2) application of this modified ratemaking structure including the modifications described in DW 16-806 and DW 19-084; and (3) application of ratemaking models assuming that PAC were still an investor-owned utility. PAC's requested rate relief is based upon the DW 16-806 and DW 19-084 modified ratemaking structures.

**Q. Mr. Goodhue, how do the rates resulting from applying the DW 16-806 and DW 19-084 modifications to PAC's ratemaking structure compare to the rates that would result from application of the existing modified ratemaking structure approved by the Commission in DW 11-026?**

A. As indicated in Mr. Ware's testimony and on Exhibit DLW-1, Tab 12 (Customer Impact), the projected aggregate revenues estimated to be allowed under the current modified ratemaking methodology (DW 11-026) would be $820,922, a percentage increase over the test period revenues of 6.35%. In contrast, as shown on the same Exhibit, the projected aggregate revenues estimated to be allowed when the DW 16-806 and DW 19-084 modifications are applied (including the implementation of the Material Operating Expense Factor, or MOEF) would be $862,927, a percentage increase over the test period revenues of 11.18%. This overall increase, for the seven- year period from the last test year of 2013, through the test year for this case of 2019, is approximately 1.5% per annum, compounded, which is at or below the annual rate of inflation for the region for that period of time.

**Q. If the current DW 11-026 methodology would result in a 6.35% increase, why are you asking the Commission to modify the methodology which results in a 11.18% increase?**

**A.** The current ratemaking methodology does not permit PAC to pay its obligations. As I described in my testimony above, PAC's depreciation lives are well in excess of its debt instrument lives. This means that the cash flow generated from depreciation does not fully meet the principal repayments on issued debt. Additionally, the new methodology is needed to: (1) insure adequate EBITDA coverage for PAC, as it relates to covenant requirements for itself or a member of the consolidated corporate group, for which is its source of working capital and intercompany loan funding, (2) provide adequate cash flows from revenues to pay debt service, CBFRR and operating expenses, and (3) provide adequate support funds in the form of the RSF accounts, to provide for cash funding during times of revenue shortfalls and expense growth above inflationary levels between rate case filings. In summary, if PAC continues to operate under the current DW 11-026 ratemaking methodology, the Company will become financially insolvent, especially as it relates to possible capital project needs in the immediate future of a material nature, for which its current rate structure would not provide adequate cash resources to support and repay.

**Q. Mr. Goodhue, can you provide a projection of how PAC's rates would increase under the proposed modified ratemaking methodology in the future?**

**A.** The Company anticipates rates would increase at approximately the rate of inflation going forward. This is based upon the following assumptions: (1) the CBFRR revenues of the Company will remain at a fixed level until 2042, (2) normal operating expenses will increase at approximately the rate of inflation, (3) property taxes may continue to increase at rates of inflation or greater per annum, and (4) the Company will be investing \$100,000-\$150,000 annually on capital and infrastructure improvements, at borrowed interest rates of between 2.5-4.5%, with the exception of the new tank anticipated for construction in 2022 at an estimated cost of \$800,000, as well as enhancements to its water treatment facility to meet NHDES and Environmental Protection Agency ("EPA") regulations in that same year at a cost of approximately \$200,000. These increases would be supported in the new rate structure under the DSRR component of the allowed revenues, and then "trued-up" for increases in operating expenses with rate cases filed about every 3 years, to reset permanent rates, and to refill or refund monies from the RSF accounts. Unlike PWW or PEU, PAC is not seeking a QCPAC program. This is because PAC plans to time the completion of its major capital projects, which are over and above "run rate" capital project investments in the next anticipated test year, for which temporary rates or a step increase could be sought, with expected increases in fully-reconcilable permanent rates in future rate case.

**Q. How would these projected resulting rates compare to the rates that would likely have resulted under private ownership?**

A. These rates would continue to be lower than rates under private ownership as a subsidiary of a publicly-traded investor owned utility. This is based upon the fact that the Company's cost of debt is only 2.5-4.5% currently, whereas under that ownership structure, PAC earned a ROE of approximately 16% pre-tax (at corporate tax rates at that time, approximately 12% at current corporate tax rates), on approximately 50% of its investments in infrastructure.

**Q. Has PAC prepared a cost of service study in connection with this filing?**

A. No. PAC is not seeking any change in rate design in this proceeding. There have not been any significant changes in the composition of PAC's customer base, and therefore PAC does not believe that a Cost of Service Study is required.

**Q. Has PAC provided PAC's payroll figures?**

**A.** PAC does not have its own employees. Instead it pays PWW a management fee under which PWW provides employee services to PAC. The management fee is shown in Tab 12 at Sch 1 Attach C, Page 2.

**Q. Will PAC be seeking a temporary rate increase?**

A. Yes. PAC will be seeking temporary rates at current rates, as indicated earlier in this testimony. The Company is filing for this to preserve its rights to full recoupment of new permanent rates back to the statutorily allowed timeframe calculated from the date of notice to customers. The Company is not seeking any temporary rate relief above its current rates. The basis for the temporary rate request is described in separate testimony to be offered jointly by Mr. Ware and me that supports PAC's petition for temporary rates.

## VIII. NOTICE TO CUSTOMERS

**Q. Please describe PAC's efforts to communicate with the affected communities and customers relative to this filing.**

A. As a matter of normal practice PAC will be communicating in writing with officials at the Town of Pittsfield contemporaneous with the filing of this case. This communication will be including the Town Manager of Pittsfield, as well as the slate of State Senators and Representatives for that community. This communication was not done prior to this filing due to certain limitations on effect and timely communication during this period of COVID-19 alternate operations for the Company and the community served.

Accompanying the required notice to customers, which will be sent to customers in conformity with the regulations after this case is filed, we will be sending a Frequently Asked Questions ("FAQ") document providing information about PAC's rate increase request.

## IX. REQUIRED APPROVALS AND CONSENTS

**Q. Would you please identify any approvals and consents required to affect the rate relief and proposed modifications to PAC's ratemaking structure?**

**A.** The principal approval required to effect the requested permanent rate relief and proposed modifications is the approval of this Commission under RSA 378:8 and :28. The requested rate relief and proposed modifications have already been addressed and approved in overall intent and concept by PAC's and Pennichuck's Board of Directors.

## X. JUST AND REASONABLE FINDING AND CONCLUSION

**Q. Mr. Goodhue, do you believe that PAC's proposed rate relief and application of the modifications to the ratemaking structure described in DW 16-806 and DW 19-084 will result in just and reasonable rates?**

**A.** Yes. I believe the requested rates and the proposed modifications are just and reasonable for several reasons.

First, the requested rates, including the effects of the proposed modifications to PAC's ratemaking structure, are generally consistent with the long-term projections presented in DW 11-026, which assumed an average annual increase in rates of approximately 3% and with the fundamental premises underlying the Commission's approval of the City of Nashua's acquisition of Pennichuck and its utilities. While the rate increase requested in this proceeding, which reflects the cumulative revenue and operating requirements of seven years with no permanent rate relief, is significant, when the cumulative increase is examined as an average annual increase, it is generally consistent with, or is actually below, the original assumptions of the acquisition docket, giving consideration to the fact that property taxes have increased at a rate above levels contemplated at that time.

Second, the requested rates continue to be lower than the levels that are reasonably projected to result from continued private investor ownership under the pre-acquisition structure. This benefit to ratepayers, which was one of the principal reasons for the approval of the City's acquisition, is due in large part to the fact that PAC has been migrating to a utility that will finance all of its material capital needs by the issuance of debt, which results in a materially lower weighted cost of capital than a private investor-owned utility with a more traditional debt and equity capitalization.

Third, the requested rates are necessary to maintain PAC's ability to continue to provide safe and high-quality water service, by financing continued reasonable and prudent operations and by having access to borrowed funds necessary to finance required capital assets and infrastructure.

Fourth, the requested modifications to PAC's current ratemaking structure are the result of a careful examination of the experience obtained through the multiple major debt financings completed for its sister subsidiary, PWW, as well as covenant compliancy issues experienced by both PWW, PEU and its parent Pennichuck Corporation. This experience allowed PWW to develop the specific modifications proposed and approved in DW 16-806 and DW 19-084, and further to have confidence that these modifications will enhance the ability of PWW, PEU and PAC to access debt markets and/or term loans in the future at affordable interest rates and at reasonable covenants. In some ways, this experience was an important prerequisite to developing the specific proposed enhancements, which is why PWW pursued the modified rate structure first in DW 16-806 and further modified it in DW 19-084, with the full expectation that this methodology would then be applied to both PEU and PAC in their next rate case filings.

Fifth, based on the ratemaking schedules filed by PAC as part of this rate case, the requested rates will demonstrably enable PAC to generate sufficient cash flows to support its ongoing operational and capital needs, as well as service its existing outstanding debt obligations.

**Q. Mr. Goodhue, do you believe that the requested rate relief and adoption of the proposed modifications are required to ensure that PAC continues to be able to provide safe and high-quality water service to its customers?**

**A.** Yes. PAC's current ratemaking structure only provides a fixed coverage component in the revenue requirement for the repayment of principal and interest to the City of Nashua under the CBFRR. Without an equity return allowable to the Company, PAC does not have a rate structure which ensures adequate cash flow coverage to cover all of its remaining operating expenses and the repayment of principal and interest on the balance of its debt obligations. This is further exacerbated by the fact that the cash flow generated from depreciation under the return on rate base is funded by assets with an average composite life of approximately 39 years, with some assets at 85 year lives. This cash flow is what is intended to provide the cash flow to repay the principal on debt used to fund the investment in rate base. However, the maximum life of debt available to PAC is 30 years. As such, the cash flow from depreciation is insufficient to cover the principal repayment cash flow requirements. Additionally, without the free cash flow generated by a return on equity, when PAC experiences reductions in revenue related to weather related and other consumption anomalies, or its expenses increase over time associated with inflation or other pressures, its revenues are not sufficient to meet the fixed operating expenses of the Company. The cost of debt service for PAC, even at favorable interest rates to the long term benefit of ratepayers, coupled with the increase of operating expenses due to normal inflationary pressures, as well as increases above inflationary levels for certain expense items (i.e. State and local property taxes), has and/or will create a mismatch between the cash flow generated from a normal allowed rate of return and depreciation expense on rate base, to the coverage of the cash flow requirements of PAC's principal and interest payments and normal operating expenses. This inherent mismatch which exists for PAC under the existing ratemaking structure (as a nearly 100% debt financed entity), coupled with the regulatory lag of obtaining rate relief 12-18 months after a given test year and a typical time frame of three years between rate cases has created and will continue to result in the revenues allowed from traditional ratemaking being insufficient to generate the necessary operating cash flows required to cover all of the Company's operating expense and debt service needs, now and into the future. The requested rate relief and proposed modifications to PAC's ratemaking structure are precisely targeted to correct these deficiencies.

**Q. Mr. Goodhue, does this conclude your testimony?**

**A.** Yes, it does.