# TAB 12

**Petition for Further Modification of Ratemaking Structure**

**STATE OF NEW HAMPSHIRE**
**PUBLIC UTILITIES COMMISSION**

Docket No. DW 20-156

PENNICHUCK EAST UTILITY, INC.

Permanent Rate Proceeding

**PETITION FOR FURTHER MODIFICATION TO RATEMAKING STRUCTURE**

Pennichuck East Utility, Inc. (PEU), in accordance with N.H. Admin. Rule Puc 203.06 (relative to petitions) and N.H. Rev. Stat. Ann. 378:28 (relative to permanent rates), and N.H. Rev. Stat. Ann. 365:28 (relative to modification of orders) hereby requests that the New Hampshire Public Utilities Commission (Commission) grant further modifications to PEU's ratemaking methodology, as described below. In support of its petition, PEU states:

**Background**

1. PEU is a regulated utility pursuant to RSA 362:4 and provides water service to approximately 8,251 customers in the towns of Atkinson, Barnstead, Bow, Chester, Conway, Derry, Exeter, Hooksett, Lee, Litchfield, Londonderry, Middleton, Pelham, Plaistow, Raymond, Sandown, Tilton, Weare, and Windham. PEU is a subsidiary of Pennichuck Corporation, which is wholly owned by the City of Nashua (City).

2. On September 23, 2020 PEU filed its notice of intent to file rate schedules, pursuant to N.H. Code Admin. R. PART Puc 1604.05. Pursuant to Puc 1604.05, utilities must give the Commission 30-days notice of its rate changes and must file any full rate case within sixty days of filing the notice of intent. The thirty-day filing window commenced Friday, October 23, 2020. Sixty days from the filing of the notice of intent is Sunday, November 22, 2020, however, pursuant to N.H. Code Admin. R. 202.03 (computation of time), that deadline is Monday, November 23, 2020.

3. Contemporaneous with this petition, and pursuant to PART Puc 1604, PEU is filing its supportive teastimony, filing requirement schedules, rate of return schedules, full rate case schedules, tariffs, and rate case expenses summary prior to the November 23, 2020 deadline. Pursant to rate schedules prior to the November 23, 2020 deadline and, pursuant to RSA 378:3, the rate filing sets in motion PEU's increase in its rates. Those rates are based on PEU's calculation of its revenue requirement. Pursuant to RSA 378:1 and RSA 378:3, the rate filing sets in motion PEU's increase in its permanent rates after the thirty day's notice. Those rates are based on PAC's calculation of its revenue requirement.

**History of Evolution of Ratemaking Methodology**

4. In Order No. 25,292 (November 23, 2011), in Docket No. DW 11-026, the Commission approved the acquisition of PEU's parent company, Pennichuck Corporation, by the City. That acquisition was completed on January 25, 2012, whereby Pennichuck Corporation ceased to be a publicly traded company. The City became Pennichuck Corporation's sole shareholder with a "limitation on Nashua's ability to draw dividends or other distributions from Pennichuck Corporation" (Order No. 25,292 at page 45). That limitation means there is no ability to sell stock and Pennichuck Corporation and its affiliates no longer have access to the equity markets for financing; they only have access to debt.

5. As part of the acquisition, the Commission approved a modified ratemaking structure for Pittsfield Aqueduct Company, Inc. (PAC), PEU, and Pennichuck Water Works, Inc. (PWW). That modification enabled those regulated utilities to earn a reasonable return on invested assets through a ratemaking methodology that still produced just and reasonable customer rates, as required under *FPC v. Hope Natural Gas*, 320 U.S. 591, 602-603 (1944). The ratemaking structure included a City Bond Fixed Revenue Requirement (CBFRR) for an equity-related item

called the Municipal Acquisition Regulatory Asset (MARA). The latter was an equity-related item approved in the revenue requirement and represented the excess of the City's purchase price over the book value of the assets of Pennichuck Corporation. The purchase price was equal to the price the City paid for the shares including all transaction and debt financing cost plus all of the existing liabilities assumed. This aggregate MARA is allocated among the Pennichuck Corporation subsidiaries, including the regulated utilities PAC, PEU, and PWW. In addition, the ratemaking structure included a $5,000,000.00 Rate Stabilization Fund (RSF) designed to provide assurance to creditors that Pennichuck Corporation's regulated utilities would meet the City's bond repayment requirements. *See Joint Petition of Nashua, Pennichuck Corporation, et al*, Order No. 25,292 at 30 (November 23, 2011) ("the fund is intended to provide holders of the City Acquisition Bonds with reasonable assurances of the available cash to be used to pay debt service on the City Acquisition Bonds, similar to a debt service reserve fund, and will hence facilitate Nashua's ability to borrow funds at reasonable interest rates, which will directly benefit customers in the form of a lower cost of capital").

6. The Commission modified the unique ratemaking structure in PAC, PEU, and PWW's 2013 rate cases. See Docket Nos. DW 13-128, DW 13-126, and DW 13-130, respectively. In those proceedings, the Commission established, among other things, the value of equity-related items and determined how the return on equity would be calculated. See Order No. 25,695 for PAC dated July 22, 2014; Order No. 25,696 for PEU dated July 25, 2014; and Order No. 25,693 for PWW dated July 15, 2014. The Commission also approved the settling parties' resolution of what constituted non-revenue producing assets, the amount of eminent domain costs, and final actual total of the MARA. *Id.*

7. In Docket Nos. DW 16-806 for PWW's general rate proceeding and DW 17-128 for PEU's general rate proceeding, and with the aid of additional years of experience with the unique ratemaking structure, the Commission again approved further modifications. In particular, the Commission approved operating expense revenue requirement components: (a) Material Operating Expense Revenue Requirement (MOERR); and (b) Non-material Operating Expense Revenue Requirement (NOERR)[1]. The Commission approved debt service revenue requirement components: (a) Debt Service Revenue Requirement-1.0 (DSRR-1.0), and (b) Debt Service Revenue Requirement-0.1 (DSRR-0.1)[2]. Similar to the rate stabilization fund for the CBFRR, the Commission approved rate stabilization funds for the MOERR (MOERR-RSF) and DSRR-1.0 (DSRR-1.0-RSF). It is relevant to note that the creation of these additional RSFs involved reallocating the original $5,000,000.00 imprest value of the CBFRR RSF among PAC, PEU, and PWW as well as allocating to the newly-created RSFs.[3] See Order No. 26,070 for PWW dated November 7, 2017 and Order No. 26,179 for PEU dated October 4, 2018. The Commission also approved a five-year average test year period for PEU and PWW. *Id.* The ratemaking modifications were designed to provide: 1) stability to customer rates, 2) assurance to creditors of PEU and PWW's ability to effectively meet cash obligations, 3) sufficient cash-flow coverage for PEU and PWW's operating needs, and 4) enhancement to PWW's credit rating. All of which

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[1] The MOERR consists of all of the operating expenses included in an Operating Expense Revenue Requirement (OERR) with the exception of those expenses specified as Non-Material Operating Expense Revenue Requirement items.

[2] The DSRR-0.1 is intended to provide a 10% over-cover for annual debt service obligations in order to satisfy debt lending requirements.

[3] Initially, $1.08 million of the original $5 million RSF was allocated to PEU and PAC ($980,000 of which was subsequently allocated to PEU in Docket No. DW 17-128) to assist those utilities in meeting their cash needs. The remaining $3.92 million of the original RSF retained by PWW was then apportioned among three reserve funds to provide additional coverage for the specific cash flow needs in its modified revenue requirement: (1) CBFRR-RSF (PWW's obligation relative to the City's acquisition bond) – $680,000; (2) MOERR-RSF (PWW's material operating expenses) – $2,850,000; and (3) DSRR-1.0-RSF (PWW's debt service requirements) – $390,000. The re-apportionment of PWW's RSF funds was specifically designed to provide stability to customer rates even under adverse conditions, as it could draw on those funds to meet its cash obligations under such conditions.

were anticipated to increase the ability to access the credit markets and obtain lower-cost debt financing.

8. Most recently, in Docket No. DW 19-084, the Commission approved additional changes to the ratemaking structure for PWW which included the addition of a Material Operating Expense Factor (MOEF) to the MOERR. See Order No. 26,383 for PWW dated July 24, 2020. PEU seeks this change to its ratemaking structure in this instant rate proceeding.

**Why the Ratemaking Changes are Necessary for PEU**

9. The reasons for the modifications to PEU's ratemaking structure are detailed in the testimonies of Mr. Larry Goodhue and Mr. Donald Ware. As the Commission is aware, the Pennichuck Corporation's regulated utilities are nearly exclusively debt-weighted in their capital structure. Although this form of capital is cheaper than equity and, ultimately, benefits ratepayers, the major credit rating agencies have been cautious in their evaluation of PWW, and likewise by the internal credit committees of the lending institutions to PEU, as the regulated utilites navigate the new capital structure and ratemaking methodologies. In discussions with the PWW's investment bankers about these modifications to the ratemaking structure, as well as discussions with the lending representatives of PEU's primary bank lender, the Company concluded that the modifications would increase access to the credit markets or commercial bank lending institutions, and most likely at an enhanced credit ratings for PWW, as well as expand access to lower cost debt for PEU, which in turn benefits customers. In general, if lenders have reasonable expectations that future rates will be more directly related to the Company's long-term, post-acquisition debt-based capital requirements and create sustainable cash coverage, then they will continue to lend to the Company to meet its ongoing capital and working capital needs, and lend to the Company and its Parent on more beneficial terms. Because PEU obtains a

significant portion of its financing as inter-company advances and loans for essential operating expenses and usage of PWW labor and equipment, the benefit of the lower credit rating PEU's affiliates obtain also flows through to PEU and its customers. Therefore, the same arguments the companies made for PWW's adoption of the modifications to the ratemaking structure also apply to PEU.

10. The need for the requested ratemaking structure modifications is readily illustrated in PEU's schedules. See Puc 1604.08 schedules at rate filing Tab 14 (Schedule 5 and Schedule 6). PEU currently has approximately $3 million in outstanding intercompany loans, as well as approximately $5 million in outstanding intercompany advances. As explained by Messrs. Goodhue and Ware, PEU presently lacks a revenue mechanism to enable it to repay its debt. This lack of cash flow is analogous to PWW's situation explained in Docket No. DW 19-084 where PWW experienced a significant draw-down of its operating expense rate stabilization fund. Similarly, PEU drew the $898,000 imprest value of its MOERR RSF down to values that approached zero. Clearly, a mechanism is needed to address this vulnerability in PEU's revenue requirement methodology**

11. To address the cash coverage concerns and the intercompany loan issue, as well as to bring uniformity as to how the revenue requirements are calculated for all Pennichuck Corporation regulated utilities (as was originally envisioned in the acquisition docket, DW 11-026, and in the 2013 rate cases), PEU requests that the Commission modify PEU's present ratemaking structure (which was approved in DW 17-128) to include:

(1) a MOEF to provide for ongoing cashflow support for PEU's MOERR and associated RSF;

(2) for atypical years in the 5-year average of water consumption, that the Company be allowed to substitute the data from the next most recent preceding typical operating year's data. Also, that an "atypical" year be defined as one in

which that year's water consumption either exceeds or falls short of the calculated trailing 5-year average of water consumption by more than 15%. Further, for purposes of determining whether an "atypical" year exists, that calculation shall be based on the trailing 5-year average of the test year as well as the four immediately preceeding years. Therefore, the underlying trailing 5-year average data used in that determination shall be inclusive of the data pertaining to the potential "atypical" year;

(3) actual NH Business Enterprise Tax cash payments in the revenue requirement;

(4) prioritization of usage of available DSRR-0.1 funds;

(5) recovery of State Revolvoing Loan Fund and Drinking Water Groundwater Trust Fund debt issuance costs; and

(6) re-establishment of imprest levels of RSF accounts retention of a previously approved reconciliation mechanism.

**Conclusion**

12. In light of PEU's revenue deficiency, its need for adequate and sustainable cash flow, PEU respectfully requests the Commission allow it to modify its ratemaking structure with the above-described targeted changes and charge rates based on that ratemaking structure.

WHEREFORE, Pennichuck East Utility, Inc. respectfully requests the Commission:

A. Grant this petition for further modification of PEU's ratemaking structure; and

B. Grant such other relief as is just and equitable.

Respectfully submitted,

PENNICHUCK EAST UTILITY, INC.

By its Attorneys,

N.H. Brown Law, PLLC

Date: November 23, 2020

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Certificate of Service

I hereby certify that on this day, a copy of this petition has been emailed to the Docket-Related Service List for this proceeding.

Date: November 23, 2020

Marcia A Brown

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