STATE OF NEW HAMPSHIRE

BEFORE THE

PUBLIC UTILITIES COMMISSION

Petition of Pennichuck East Utility, Inc. for Approval of Financing From CoBank, ACB

DW 21-___

DIRECT PREFILED TESTIMONY OF LARRY D. GOODHUE

September 2, 2021

Q. What is your name and what is your position with Pennichuck East Utility, Inc.?

A. My name is Larry D. Goodhue. I am the Chief Executive Officer and Chief Financial Officer of Pennichuck East Utility, Inc. (the "Company" or "PEU"). I have been employed with the Company since December 2006. I also serve as Chief Executive Officer and Chief Financial Officer of the Company's parent, Pennichuck Corporation ("Pennichuck"). I am a licensed Certified Public Accountant in New Hampshire; my license is currently in an inactive status.

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.

Q. Please describe your professional background.

A. Prior to joining the Company, 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 in several companies.

Q. What are your responsibilities as Chief Executive Officer and Chief Financial Officer of the Company, and Chief Executive Officer and Chief Financial Officer of Pennichuck?

A. Including my primary responsibilities as Chief Executive Officer, with ultimate responsibility for all aspects of the Company, I am responsible for the overall financial management of the Company including financing, accounting, compliance and budgeting. My responsibilities include issuance and repayment of debt, as well as quarterly and annual financial and regulatory reporting and compliance. I work with the Chief Operating Officer (COO) of the Company to determine the lowest cost alternatives available to fund the capital requirements of the Company, which result from the Company's annual capital expenditures and its current debt maturities. Additionally, I work with the COO to determine optimum opportunities to fund and support the Company's rate structure elements, including its Rate Stabilization Funds (RSFs), in bringing about the most advantageous overall structure for current and future customers rates.

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 Pennichuck East Utility, Inc. – DW 12-349, DW 13-017, DW 13-125, DW 14-020, DW 14-191, DW 14-282, DW 14-321, DW 15-044, 16-234, DW 17-055, DW 17-157, DW 18-101, DW 18-132, DW 19-069, DW 19-112, DW 20-081 and DW 21-102;
- Financings for Pennichuck Water Works, Inc. – DW 14-021, DW 14-130, DW 15-046, DW 15-196, and DW 16-236, DW 17-183, DW 18-133, DW 19-026, DW 20-055, DW 20-064, and DW 20-157;

- Financings for Pittsfield Aqueduct Company, Inc. – DW 15-045, and DW 16-235, and DW 18-033;
- Permanent and Temporary Rate Increase Proceedings for: Pennichuck Water Works, Inc. – DW 13-130; DW 16-806 and 19-084; Pennichuck East Utility, Inc. – DW 13-126, DW 17-128 and DW 20-156; and Pittsfield Aqueduct Company, Inc. – DW 13-128 and DW 20-153.

Q. What financings are proposed by the Company in its petition in this proceeding (the "Proposed Financing").

A. The Company is proposing one new debt financing: a term loan for $2,546,632 from CoBank, ACB ("CoBank") to fund the "one time" refill and replenishment of the Company's Rate Stabilization Fund (RSF) funds to their imprest levels, specifically the Material Operating Expense Revenue Requirement (MOERR RSF), in conjunction with the new permanent rates and modified rate structure seeking approval for the Company in Docket No. DW 20-156, currently open and in pendency with the Commission. This request is directly tied to that open Docket, which if approved, is intended to insure that this is a "one time" replenishment of the MOERR RSF with a debt issuance such as this, as that open docket includes the establishment of a Material Operating Expense Factor (MOEF) as a part of the Company's requested modified rate structure, with that element being requested to provide the necessary operating revenues between rate cases to provide for reinforcement of the RSF funds at their near imprest levels, leading up to the next filed full rate case for permanent rate relief.

Q. Did you supervise the preparation of the Company's petition for authority to issue long term debt?

A. Yes.

Q. Does the Company have on file with the Commission a certification statement in its Annual Report with respect to its book, papers and records?

A. Yes.

Q. Mr. Goodhue, before explaining the details of the proposed financings, would you like to provide some history regarding the ownership of PEU and how that history supports this request for financing approval?

A. Yes. Currently, PEU is a wholly owned subsidiary of Pennichuck, which is, in turn, wholly owned by the City of Nashua, New Hampshire (City). The City acquired its ownership of Pennichuck on January 25, 2012, pursuant to this Commission's Order No. 25,292 (November 23, 2011) (Approving Acquisition and Settlement Agreement). Prior to this acquisition by the City, Pennichuck's shares were traded on a public stock exchange (the NASDAQ exchange). This change in the ultimate ownership of PEU's parent, Pennichuck, from a publicly traded shareholder ownership to ownership by the City has had important consequences for the operation of PEU.

One of the consequences is that PEU, after the City's acquisition of Pennichuck, no longer has access to private equity markets, thru its parent company, as a method of financing its capital needs. As contemplated by deliberations during the Commission's proceeding to approve the City's acquisition of Pennichuck in DW 11-026, after the acquisition, PEU was expected to finance its on-going capital needs entirely through the issuance of debt. One result of this anticipated debt financing is that the weighted average cost of PEU's capital is significantly lower than it was prior to the City's acquisition. This lower cost of capital has direct benefits for PEU's customers. Under the docket for DW 17-128, the Company provided support for its existing capital structure, for which approval was granted for a modified rate setting methodology in Order No. 26,179. This financing petition is directly related to the Company's current debt needs, as well as a structure that is in full support of that modified rate methodology, and as being requested for further modification in Docket No. DW 20-156.

Q. Please explain the purpose of the proposed CoBank term loan financing.

A. During 2021, as the process of deliberating the permanent rate case for the Company progresses in Docket No. DW 20-156, the Company considered alternatives that might be available to provide for the needed cash to refill its fully depleted MOERR RSF, along with the reallocation of over-collected funds in the CBFRR RSF and DSRR RSF accounts. In fact, during that proceeding, it has been demonstrated that the MOERR RSF has not only been fully depleted, but actually overdrawn with those amounts being funded and supported by borrowings from the Pennichuck Corporation Working Capital Line of Credit, thru its senior commercial lender. The alternative offered in the filing of that case and docket, was the replenishment of the MOERR RSF funds with a deferred asset to be amortized into rates over a period of 10 years, including the implementation of the MOEF at a 6% factor level. However, during discovery with the parties to the case, the Company included discussions with the parties one of the other alternatives it had considered and was actually requested to be considered in lieu of that deferred asset methodology. The alternative was the ability to "one time" fund the RSF shortfall with external debt for a 25-year period of repayment. Therefore, this financing is the

Company's attempt to meet the Company's financial needs and address party concerns over rate shock. Specifically, the Company will fund the shortfall funds needed to allow for the implementation of the MOEF in this case at a 4% level (with the full 6% level being sought in the Company's next permanent rate case proceeding), with a term loan for 25 years. The Company is hopeful that a settlement agreement between the parties will occur in the rate case that integrates the results of this financing, if the parties do not choose in settlement to proceed ahead with the originally offered methodology for refilling the RSF funds, and implementing the MOEF at its full requested and required level. Pursuing this as an alternative to the deferred asset approach would result in current savings in the new permanent rates being requested, of approximately 3.37% (an estimated 16.47% versus and estimated 19.84%), primarily due to the impact of a 25-year amortization versus a 10-year amortization, which spreads the overall value of that recovery over that longer timeframe, but on a different economic basis. The reason that the savings that would be accomplished is an estimate, is that the actual interest rate on the loan would not be known for certain until the loan is funded and closed, as the interest rates float with market rates until they are locked in.

Q. Please describe CoBank and its relationship with the Company.

A. CoBank is a federally chartered bank under the Farm Credit Act of 1971, as amended. Unlike commercial banks and other financial institutions, it is restricted to making loans and leases and providing financial solutions to eligible borrowers in the agri-business and rural utility industries and certain related entities as defined under the Farm Credit Act of 1971. The characteristics of the Company's service territory are consistent with

CoBank's charter and mission, and CoBank can therefore provide short, intermediate and long-term loans to the Company in connection with its capital requirements. The Company entered into a Master Loan Agreement with CoBank effective February 9, 2010 (the "Master Loan Agreement"), which provides the framework for CoBank to make loans to the Company from time to time. The Master Loan Agreement was filed with the Commission in Docket No. DW 09-134. In March 2010, the Company utilized CoBank to replace $4.5 million of maturing debt and to establish a $1.5 million revolving line of credit pursuant to Order No. 25,041 in Docket No. DW 09-134. The $1.5 million revolving line of credit expired in March 2012. Additionally, in May 2013, the Company entered into two new loans with CoBank, in the amount of $925,000 and $1,723,150, for terms of 20 years and 10 years, respectively, pursuant to Order No. 25,480 in Docket No. DW 13-017. Also, the Company entered into a new loan with CoBank in March 2015, in the amount of $625,000, for a term of 25 years, pursuant to Order No. 25,746 in Docket No. DW 14-282; another loan with CoBank for $2.2 million for a term of 25 years, pursuant to Order No. 25,890 in Docket No. DW 16-234; another loan with CoBank for $350,078 for 25 years, pursuant to Order No. 26,117 in Docket No. DW 17-157; another loan with CoBank for $1,153,000 for 25 years, pursuant to Order No. 26,253 in Docket No. DW 19-069; and another loan with CoBank for $800,122 for 25 years, pursuant to Order No. 26,418 in Docket No. DW 20-081. And lastly, the Company is awaiting the closing on its most current loan with CoBank, for $1,135,409, as approved pursuant to Order 26,507 in Docket No. DW 21-102, at some time in late September after the Order NISI for that loan becoming fully effective on or after September 10, 2021.

CoBank is a Government Sponsored Enterprise ("GSE") owned by its customers, who consist of agricultural cooperatives, rural energy, communications and water companies and other businesses that serve rural America. As a GSE, CoBank issues its debt securities with the implicit full faith and credit of the US Government and uses these low-cost funds to make loans to businesses like the Company that meet its charter requirements. As a result of the implicit backing of the US Government, CoBank's borrowing costs are less than commercial banks and financial institutions and the lower costs are passed on to its borrowers. In addition to the lower rates, CoBank loans generally have fewer covenants or restrictions as compared to loans from commercial banks and other financial institutions.

Q. What are the basic terms of the proposed CoBank term loan financing?

A. While the final terms and interest rates are subject to change based on CoBank's due diligence (which is in progress) and market conditions, the Company expects to obtain a $2,546,632 term loan with a 25-year amortization, with level monthly principal and interest payments with an interest rate to be determined based on market conditions (currently estimated at 4.5% per annum). The proceeds from this new CoBank loan will be used to refill the Company's MOERR RSF to its full imprest level and repay the excess funds that were borrowed from Penn Corp's W/C Line of Credit, as fully described and included in schedules in support of the Company's rate case proceeding, as it pertains to this parallel activity to that proceeding. The new CoBank loan will be secured by (i) a security interest in the Company's equity interest in CoBank (consisting of the Company's $212,825.39 equity investment in CoBank and the Company's right to receive patronage dividends) and (ii) the unconditional guarantee of the Company's obligations to CoBank by Pennichuck pursuant to the Guarantee of Payment by Pennichuck in favor of CoBank dated as of February 9, 2010 (the "Guaranty"), a copy of which was also filed with the Commission in Docket No. DW 09-134. The Company's equity investment in CoBank consists of an initial $1,000 investment pursuant to the Master Loan Agreement cited earlier, as well as the accumulation of the equity portion of the annual patronage earned by the Company, associated with its existing debt obligations with CoBank. A copy of CoBank's Non-Binding Summary of Terms and Conditions is attached as LDG-4, and subject to confidential protection, for which a motion is being provided.

Q. Are there any other important terms or benefits related to borrowing from CoBank?

A. Yes, as I mentioned earlier, CoBank is organized as a cooperative which means it is owned and controlled by its members who use its products or services (i.e. its borrowers). A key cooperative principle is the return to customers of a portion of net margins based upon their use of the bank. This is accomplished through the distribution of "patronage refunds" which are a distribution to patronage customers of net margins remaining after payment of preferred stock dividends, deducting operating and interest expenses and amounts retained as core surplus. While not guaranteed, each year the Board of Directors of CoBank targets a distribution amount which is returned (in the subsequent year) to its borrower/members based on the annual average accruing loan volume. While these "patronage" payments are not guaranteed, the Company expects to reflect the patronage refunds in rates in future test years based on the receipt of the payments. The Company's experience with patronage refunds associated all of the current amounts borrowed from CoBank, as highlighted earlier in this testimony, is as follows:

- 2010 earned patronage of $37,355,
- 2011 earned patronage of $43,108,
- 2012 earned patronage of $41,482,
- 2013 earned patronage of $57,351,
- 2014 earned patronage of $63,638,
- 2015 earned patronage of $66,012,
- 2016 earned patronage of $ 71,432,
- 2017 earned patronage of $20,706,
- 2018 earned patronage of $26,359,
- 2019 earned patronage of $30,575, and
- 2020 earned patronage of $62,574

In general, CoBank's annual patronage has been 1% of the one-year average daily loan balance, paid to the Company in March of the following year (i.e. patronage earned in calendar year 2020 was paid to the Company in early April 2021). The 1% is distributed as a mix of cash and equity stock in CoBank; for the years 2010 and 2011, the mix of cash and equity was 35% and 65%; whereas for the years 2012 thru 2017 the mix of cash and equity was 75% and 25%; for the year 2018 the mix was 60% and 40%; for the year 2019 the mix was 65% and 35%; for the year 2020 the mix was 66.8% cash and 33.2% equity. The Company accounts for the cash portion as a reduction in interest expense when received in accordance with GAAP. The equity portion is accounted for as a deferred debit on the balance sheet.

Q. What other options has the Company considered other than the proposed CoBank financings?

A. The Company has explored options with several potential funding agencies over the past several years. The Company has determined that tax exempt debt bond financing through the Business Finance Authority of New Hampshire ("BFA") lending is not available, as the overall borrowing levels for the Company do not meet the minimum bonding threshold amounts, even when aggregated over a three-year needs analysis. As evidenced in this petition, as well as petitions filed and approved in previous years, the Company has been able to access some funding from the State Revolving Fund (SRF) or the Drinking Water and Groundwater Trust Fund (DWGTF), for certain eligible and qualifying capital projects. However, even though a few significant projects in 2020 did qualify for SRF funding, not all of the Company's capital projects for 2020 were eligible for either SRF or DWGTF financing. As a result, the options to finance the remainder of the Company's capital projects was limited to taxable debt from banks or other financial institutions. For banks, the Company has determined over the past several years that there are a limited number of truly eligible lending candidates due to considerations including the financial structure of the Company with respect to normal debt-equity ratios, the overall capital borrowing needs, meeting normal financial covenants, or due to acceptable credit ratings. At the end of the process, CoBank has become the only viable option currently available to the Company to finance these current needs. This is especially true when it comes to the type of loan being requested in this filing. A term loan to refill RSF funds would not be something that would be welcomed by a lender that doesn't already have a portfolio of credits with an entity such as PEU, and as such, CoBank is the source for this type of funding, and has been evidenced by them preparing and providing a term sheet to the Company for this requested loan, as attached as LDG-4, and subject to confidential protection, for which a motion is being provided.

Q. What are the estimated issuance costs for these CoBank loans?

A. The anticipated issuance costs total less than $10,000 and relates primarily to legal costs which will be incurred to (i) review and revise the necessary loan documentation prepared by CoBank, and (ii) obtain Commission approval of the loans. The issuance costs will and amortized over the life of the CoBank loans. The annual amortization expense of $500, associated with the issuance costs, has not been reflected in Schedules LDG-1 through 3, due to its immateriality with respect to the overall analysis and impact of this proposed financing.

Q. Please explain Schedule LDG-1, entitled "Balance Sheet for the Twelve Months Ended December 31, 2020".

A. Schedule LDG-1, pages 1 and 2, presents the actual financial position of the Company as of December 31, 2020 and the pro forma financial position reflecting certain adjustments pertaining to the proposed CoBank $2,246,632 term loan financing.

Q. Please explain the pro forma adjustments on Schedule LDG-1.

A. Schedule LDG-1, page 1, reflects the pro forma adjustments to record overall impact on the RSF funds section of the financial statements as it relates to the refinancing and financing of the debt instruments included in this transaction. Schedule LDG-1, page 2: This schedule reflects the impact on the Long-term Debt section of the balance sheet, and also reflects the net income impact on retained earnings related to costs associated with the financings, as reflected on Schedule LDG-2. Schedule LDG-1, page 2, also records the repayment of intercompany funds to the extent they were used to support the MOERR RSF leading up to the current permanent rate case, and this financing request, based upon actual bank account balances as of 12/31/2020.

Q. Mr. Goodhue, please explain Schedule LDG-2 entitled "Operating Income Statement for the Twelve Months Ended December 31, 2020".

A. As indicated previously, the issuance costs associated with the financing are not expected to be significant and are not reflected in Schedule LDG-2, page 1. Schedule LDG-2, page 1, presents the pro forma impact of this financing on the Company's income statement for the twelve-month period ended December 31, 2020.

Q. Please explain the pro forma adjustments on Schedule LDG-2.

A. Schedule LDG-2, page 1, contains two adjustments. The first adjustment records the estimated increase in interest expense related to additional debt raised at interest rates of 4.5% per annum. The second adjustment records the income tax effect of the additional pro forma interest expense using an effective combined federal and state income tax rate of 27.08%.

Q. Please explain Schedule LDG-3 entitled "Projected Rate Impact on Single Family Residential Home"

A. Schedule LDG-3 illustrates the Company's pro forma impact from this financing on the average single-family residential home's water bill, as it pertains to the rates that were approved under Docket No. DW 17-128, as well as the impact as known from the DW 20-156 docket, per the 1604.06 schedules pro-formed and supplemented into that case as of 8/10/2021.

Q. Mr. Goodhue, are there any covenants or restrictions contained in the Company's other bond and debt agreements which would be impacted by the issuance of debt under this proposed financing?

A. Yes. Section 6(c) of the Loan Agreement between Pennichuck and TD Bank, NA (the "Bank") prohibits Pennichuck or its subsidiaries from incurring additional indebtedness without the express prior written consent of the Bank, except for certain allowed exceptions. One of the listed exceptions, in Section 6(c)(v) the Company may incur new indebtedness up to $1.5 million per annum, on an unsecured basis, with CoBank, ACB or equivalent lender, provided that TD Bank, N.A. is provided at least 30 days prior to written notice related to said indebtedness. Amounts borrowed from CoBank above that limit require approval from TD Bank, N.A. The Company is providing its written request to TD Bank subsequent to submitting this filing. The Company will supplement its Petition with documentation showing that request and TD Bank's approval when available.

Q. What is the status of corporate approvals for CoBank Financings?

A. The CoBank financings have been approved by the Company's and Pennichuck's Boards of Directors as documented in LDG-5 and LDG-6, and have been submitted, concurrently and in parallel, for approval by Pennichuck's sole shareholder, the City of Nashua. The Company will supplement its Petition with documentation showing the City's approval when available.

Q. Do you believe that the CoBank Financings will be consistent with the public good?

A. Yes. This CoBank loan will enable PEU to continue to provide safe, adequate and reliable water service to PEU's customers, while allowing for the implementation of the MOEF in the Company's current rate case, at rates below those initially requested. The terms of the financing through the CoBank loans are very favorable compared to other alternatives and will result in lower financing costs than would be available through all other current debt financing options. And, the overall impact of this borrowing is to provide for a modified rate structure that is more stable for rate payers and better provides for adequate cash flow coverage for the Company's necessary operating expenses.

Q. Is there anything else that you wish to add?

A. Yes. I respectfully ask the Commission to issue an Order in this docket by October 31, 2021, if at all possible, such that the Order can be effective no later than the end of November. This will allow the Company to close upon the term loan as a requirement in establishing the final permanent rates under the Company's permanent rate case in pendency in Docket No. DW 20-156. Timely closing on the CoBank term loan, will allow the Company to include the actual impact of this loan in its final approved rates in that case. Attached as Exhibits LDG-7 thru LDG-9, are schedules which were provided in discovery under Docket No. DW 20-156, as it pertains to this financing, and the impact it has in that permanent rate proceeding.

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

A. Yes, it does.