STATE OF NEW HAMPSHIRE

BEFORE THE

PUBLIC UTILITIES COMMISSION

Joint Petition of Pennichuck East Utility, Inc. and Pittsfield Aqueduct Company, Inc. for a Waiver and Increase to the Short-Term Debt Limit

DW 23-___

DIRECT PREFILED TESTIMONY OF GEORGE TORRES

June 26, 2023

Q. What is your name and what is your position with Pennichuck Eat Utility, Inc. and Pittsfield Aqueduct Company, Inc.?

A. My name is George Torres and I am the Chief Financial Officer, Treasurer and Corporate Controller of Pennichuck East Utility, Inc. and Pittsfield Aqueduct, Inc. (the "Companies" or "PEU" or "PAC"). I have been employed with the Companies since February 2006, when I initially served as the Corporation's Accounting Manager. In 2015, I assumed the role of Director of Accounting and Corporate Controller, and was named and appointed as Treasurer in May 2020, in addition to those roles. I have assumed the role of Chief Financial Officer of the Companies as of January 1, 2023. I also serve as the Chief Financial Officer, Treasurer and Corporate Controller of the Companies' parent, Pennichuck Corporation ("Pennichuck").

Q. Please describe your educational background.

A. I have a Bachelor of Science degree in Business Administration with a major in Accounting from Montclair State University in Montclair, New Jersey.

Q. Please describe your professional background.

A. Prior to joining the Companies, I held Controller and Senior Accountant positions for several subsidiaries for the global human resource company Vedior North America, now known as Randstad USA from October 2002 to February 2006. My duties included all financial, accounting, and reporting functions for the subsidiaries as assigned. Prior to joining Vedior N.A., I held various senior accounting positions for several companies in the retail, energy services, and manufacturing sectors.

Q. What are your responsibilities as Chief Financial Officer, Treasurer, and Corporate Controller of PEU, PAC and Pennichuck?

A. I am responsible for the overall financial management of the Companies including financing, treasury, accounting and budgeting functions. My responsibilities also include issuance and repayment of debt, as well as quarterly and annual financial and regulatory reporting and compliance. The performance of these responsibilities is on the behalf of Pennichuck Corporation and all its subsidiaries. In this capacity, I work with both the CEO of the Company, and other members of the senior management team, in the performance of my duties.

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"):

- Modification of Accounting Treatment of Leases for Pennichuck Water Works, Inc. – Docket No. DW 21-137;
- Waiver/Increase of Short-term Debt Limit for Pittsfield Aqueduct Company, Inc. – Docket No. DW 22-075.
- Refinance of CoBank T4 Note for Pennichuck East Utility, Inc. – Docket No. DW 23-024
- Renewal of FALOC for Pennichuck Water Works, Inc. – Docket No. DW 23-040

- Approval of a CoBank Term Loan for Pennichuck East Utility – Docket No. 23-046
- Renewal of FALOC for Pennichuck East Utility – Docket No. 23-049
- Approval to Restructure Short-term Debt to Long-term Debt for Pittsfield Aqueduct Company, Inc. – Docket No. DW 23-061

Q. Please provide an explanation of the purpose of this written pre-filed testimony.

A. The purpose of this written pre-filed testimony is to explain the basis for the Companies' joint request for approval of a waiver of the 10% short term debt limit under N.H. Admin. Rule Puc 608.05. This request is being made in light of the pending expiration of the current waivers for both PEU and PAC, which expires on June 30, 2023. The Commission previously approved waivers and increase in the short-term debt limit through June 30, for PEU by Order No. 26,311 (November 27, 2019) and PAC by Order No. 26,823 (May 16, 2023). As a result of Order No. 25,292 (November 23, 2011) approving the acquisition of Pennichuck by the City of Nashua, the capital structure for the Companies were altered, to the benefit of ratepayers, by essentially eliminating the costs of equity financing. The resulting capital structures, however, alters the manner in which capital expenditures and working capital are funded, placing a greater emphasis on short-term debt financing for both companies. Additionally, since all capital investments are financed by debt, PAC's relatively small size limits its financing options to either SRF (State Revolving Fund) debt, DWGTF (Drinking Water and Groundwater Trust Fund) loans, or intercompany loans.

Q. What safeguards are in place to prevent abuses by the Companies.

A. The Companies will continue to include monthly levels of short-term debt with its Annual Reports. Also, monthly reporting of ratios are included in the financial reporting package submitted monthly to the Commission.

Q. Please describe the Company's recent short-term debt levels.

A. Since the Companies last approved waivers noted above that increased the short-term debt limit from 10% to 18% through June 30, 2019: (1) PEU has experienced short-term debt levels that have ranged between 8.87% and 17.37%. (2) PAC has experienced short-term debt levels that have ranged from -0.45% and up to a debt level reaching 21.3% in August 2022 due to a temporary one-time year-to-date true-up in the intercompany accounts for the Companies' balance sheet (upon the completion of the accounting for that one-time true-up and the corresponding balance of the bookkeeping for that event, the level currently sits at 19.40% as of May 2023). That joint waiver also required the Company to send a notice to the Department of Energy (DOE) and Office of Consumer Advocate (OCA) in any month exceeding 15%. The Companies did notify DOE (1) on July 28, 2022 for PEU when its short-term debt level reached 15.82%; and (2) on November 3, 2022, for PAC when its short-term debt level reached 21.30%. However, due to current and anticipated levels of short-term debt, the Companies' request a temporary short-term debt waiver and increase in the debt limit to 18% from the Commission until June 30, 2025, consistent with a joint waiver granted to the Companies in Docket No. DW15-288 (Order No. 25,820) and the more recent orders discussed above.

Q. Please explain Exhibit GT-1, entitled "PEU PAC Historical Summary of Short-Term Debt Limits".

A. Schedule or Exhibit GT-1 presents the actual short-term debt limit levels for the Companies for the period from June 30, 2019 through May 31, 2023**.** This ending date is the most current date for which the books and records of the Companies are closed and accurate reporting of the short-term debt limit levels can be provided with this filing.

Q. How does the rate making structure of PEU and PAC differ from traditional rate making, and how do the CBFRR payments impact the short-term debt limit requirements?

A. The rate making structures of PEU and PAC differs from traditional rate making in a few key areas, affecting both total cash flow and the timing of cash flows. As a consequence of the acquisition of Pennichuck by the City of Nashua, the following key changes were made:

1. A pre-determined rate was derived for the Companies' Return on Equity (ROE). The ROE is set at 3% above the 13-month average yield for 30-year Treasury bonds, for the last approved test year. This equates to a pre-tax ROE of 5.90% for both Companies for the 2012 test years approved in Dockets DW 13-126 and DW 13-128, and 2019 test year approved in DW 20-153. This ROE is substantially different from pre-tax ROE levels historically included in the rate structures of the Companies, which were approximately 16%. In addition, due to the nature of the Companies' rate and ownership structures, including the funding of the CBFRR portion of allowed

revenues as intercompany transfers of cash to Pennichuck Corporation, both PEU and PAC generally has no equity for which a ROE is earned.

2. The City Bond Fixed Revenue Requirement ("CBFRR") portion of the revenue requirements for the Companies were implemented as part of the acquisition. This fixed component of the revenue requirement for each company is that each company's proportionate share of a fixed annual funding amount of the City's Acquisition Debt paid up to Pennichuck, which enables Pennichuck to repay the City of Nashua. The cash transferred from the CBFRR revenues, net of the income tax provision on pre-tax earnings, for each fiscal year is authorized and recorded as a both a dividend and return of capital to Pennichuck in the first quarter of the year (for the prior year's aggregate amount), in order to properly account for the payment of cash related to the CBFRR revenues. The annual dividend is recorded as an offset to the short-term debt accounts of each company (as the CBFRR is a short-term cash flow component of the Company’s income from operations), which has a material annual impact on the short-term debt limit requirements.

3. The capital structures of the Companies were altered to be nearly exclusively dependent on debt, versus the traditional debt/equity ratio that existed prior to the merger. For PEU and PAC, based upon the funding sources currently available to the Companies for long-term capital investments, this requires using short-term debt to support long-term capital projects, until

long-term financing is received from external lenders such as the New Hampshire Department of Environmental Services' SRF or DWGTS loan programs, or annual term loans are approved and secured for PEU thru its primary commercial lender, CoBank.

4. A Rate Stabilization Fund (RSF) was established at the time of the City's acquisition of Pennichuck Water Works, Inc. (PWW), and has since been allocated amongst the three regulated subsidiaries: PAC, PWW, and PEU. The RSF is available for use by the Companies when actual earned revenues are below allowed revenue requirement levels. Each company has the ability to borrow from these funds, to offset the deficit in revenues for the CBFRR, OERR and DSRR portion of the revenues, and to deposit excess revenues earned above allowed revenues into the RSF funds. This movement of cash to and from the RSF funds, would serve to potentially increase or decrease the Companies' short-term debt levels over time, absent the ability to replace these amounts with equity contributions (should a deficiency in revenues exist).

Q. How will ratepayers benefit from a waiver of the 10% short term debt limit?

A. A waiver of the 10% short term debt limit will allow the Companies to better manage cash flows throughout the year, finance working capital as intended within the current rate structures, and effectively invest in long-term capital replacement projects while obtaining annual reimbursement financing for these projects through various funding sources, including CoBank, the SRF and DWGTF loans when available. If the waiver is not granted, the companies would be barred from accessing this available long-term debt financing for capital projects, which would be adverse to one of the companies' primary objectives for its customers; maintaining and properly upgrading their respective treatment and distribution facilities in order to fully comply with Safe Drinking Water Standards, on a consistent and reliable basis.

Q. **Will the waiver provide needed flexibility in the overall financing of the operations of the Companies**?

A. Yes. The Companies' currently have an extremely limited number of external long-term debt funding sources. PEU has access to funding for certain projects through CoBank as a commercial bank lender, and the SRF or DWGTF for certain eligible projects. PAC, on the other hand, only has funding available for certain long-term capital projects under the SRF or DWGTF, if in fact projects proposed are even eligible for funding in those programs, as it is of insufficient size and financial strength to qualify currently for term loans with commercial bank lenders. Accordingly, the balance of long-term capital project funding for PAC, over and above SRF and DWGTF funded amounts, comes from short-term working capital advances from Pennichuck, which can be converted into long-term intercompany loans, when and if approved by the Commission.

It is important to note that, as a rule, funds spent on long-term capital projects, using short-term advances from Pennichuck or short-term working capital of the Companies, are subject to refinance with intercompany loans approved in periodic financing proceedings before the Commission. Consequently, increasing the short-term debt limits for the Companies will enable them to fund projects in a more predictable and orderly manner, reducing or foregoing the expense of long-term financings and rate cases.

Furthermore, the waiver accommodates funding of the CBFRR payments to Pennichuck throughout the year, workorder and management fee expenses which causes a build in the short-term debt levels to Pennichuck, pending the annual dividend (described above) related to these transfers of cash.

Q. Is the purpose of Puc 608.05 satisfied by an 18% limit?

A. Yes. The short-term debt rule, which implements RSA 369:7, appears intended to limit ratepayer exposure from utility funding of long-term projects with potentially higher cost short term cash flows or debt, which, at the same time, would not properly match the cash outflows for the depreciation associated with capital expenditures to the cash inflows from the funding source. The rule sets a generic short-term debt limit, above which a utility may not issue short-term debt without Commission approval. Under the existing rate structures and circumstances of PEU and PAC, however, the 10% debt limit is unnecessarily restrictive. Inasmuch as all capital investments for the Companies will be financed by debt, and their small size limits their financing options, increasing the short-term debt limit to 18% appropriately balances the policy goals of, on the one hand, limiting ratepayer exposure to increased financing costs without prior Commission approval and, on the other hand, decreasing financing and regulatory costs by providing financing flexibility to both Companies.

Q. Do you believe that this proposal will be consistent with the public good?

A. Yes. A temporary waiver of the 10% short term debt limit and approval of an 18% short-term debt limit will serve the public interest because it will**:**

(1) Allow the Companies to effectively reinvest in long-term capital projects and infrastructure at debt funding rates as opposed to debt/equity rates, thereby lowering the overall cost to ratepayers;

(2) Provide both PEU and PAC the flexibility to effectively pursue long-term reimbursement financing in support of eligible capital projects, which allows it to pursue favorable borrowing rates, such as those associated with the SRF or DWGTF loan programs; and,

(3) Stabilize revenue levels by allowing PEU and PAC to focus on annual revenue levels, without concern of running afoul of the overly restrictive 10% short-term debt limit requirement in portions of the fiscal year.

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

A. Yes, it does.