

PUBLIC UTILITIES COMMISSION

DW 19-147

HAMPSTEAD AREA WATER COMPANY, INC.

Petition for Approval to Accept Drinking Water and Groundwater Trust Fund Grant and Financing, Bank Financing, and Motion for Bifurcation

Order *Nisi* Approving DWGTF Financing and Motion for Bifurcation

ORDER NO. 26,407

September 28, 2020

This order approves a request by Hampstead Area Water Company to borrow up to \$1,204,815 from the New Hampshire Drinking Water and Groundwater Trust Fund. This order also approves Hampstead Area Water Company's request to bifurcate its financing petition, providing more time to secure financing applicable to the Manchester Source Development Charge. This order is issued on a *nisi* basis to ensure that interested persons receive notice and have the opportunity to comment or request a hearing before the order becomes effective.

I. PROCEDURAL HISTORY AND BACKGROUND

Hampstead Area Water Company, Inc., (HAWC or the Company), is a regulated water utility providing water service to approximately 3,700 customers in thirteen towns. On September 9, 2019, HAWC petitioned for, among other things, authority to accept a grant from the New Hampshire Drinking Water and Groundwater Trust Fund (DWGTF), and a loan from the DWGTF to pay the income tax associated with receipt of that grant.¹

On October 20, 2019, the New Hampshire Department of Environmental Services (DES) filed a letter in support of HAWC's requested financing.

¹ The Tax Cuts and Jobs Act of 2017 removed the exemption for contributions in the aid of construction from taxable income previously appreciated by water utilities, effective January 1, 2018. Commission Staff, Recommendation, April 17, 2020 at 2.

On February 26, 2020, the Company filed a motion to bifurcate its financing request. HAWC, specifically, requested additional time for the Company to secure the financing pertaining to its payment of the Manchester Source Development Charge (MSDC). The MSDC is a capacity charge that applies in addition to regular water usage charges. Manchester Water Works, which is a municipal water utility not regulated by the Commission, applies the MSDC to support development of the Merrimack River as a supplemental water supply. *Town of Derry*, Order No. 26,255 at 2 (June 7, 2019). Commission Staff (Staff) filed its recommendation on April 17.

The Company's petition and subsequent docket filings, other than any information for which confidential treatment has been requested of or granted by the Commission, are posted at <http://www.puc.nh.gov/Regulatory/Docketbk/2019/19-147.html>.

II. POSITIONS

A. HAWC

HAWC petitioned for approval to borrow up to \$1,204,815 from the DWGTF (DWGTF Loan) to pay for the income tax associated with receipt of the DWGTF grant money and contributed plant from the Towns of Salem and Plaistow. HAWC initially estimated it would only need \$894,494 to pay its income tax on the contributions in aid of construction (CIAC), but requested approval to borrow a higher amount. Through discovery, it was determined that the actual tax liability is estimated at \$1,102,356. HAWC also sought: (1) authority to borrow up to \$392,500 to finance a portion of the MSDC the Company will incur; (2) authority to receive \$3,283,750 in DWGTF grant money; (3) a finding by the Commission that the proposed amounts and proceeds of the financings are prudent and consistent with the public interest; and (4) authority to increase its rates to recover its investment and earn a reasonable rate of return.

According to HAWC's petition, the financing requests and other various approvals sought relate to the Company's construction costs in Phase I of the Southern New Hampshire Regional Water Interconnection Project (Project). *See* Commission Staff Recommendation, April 17, 2020, at footnote 1 (the project is "an initiative supported by DES to transmit water supply from Manchester Water Works to the towns of Windham, Salem, Atkinson, Hampstead, and Plaistow"). HAWC noted that a substantial portion of the planning process for the Project occurred prior to the 2018 tax law change.

The Company stated that the DWGTF Loan will amortize over a 25-year period, through monthly payments, at an interest rate of 2.96 percent. HAWC further stated that interest payments are due for six months following substantial completion of Phase I construction. After that six-month term expires, the Company will make payments on the financing's principal and interest.

HAWC argued that the DWGTF Loan is consistent with the public good as the financing enables the Company to pay its income tax resulting from its participation in the Project. Once Phase I of the Project is completed, HAWC will be able to provide safe and reliable water service to its existing customers and future customers in Plaistow. In addition, the Project will provide water and emergency supply stability within HAWC's two core systems.

On February 26, 2020, HAWC filed an assented to motion to bifurcate consideration of the MSDC financing from the DWGTF Loan. The Company requested bifurcation of the financing matters to allow it additional time to secure the MSDC financing and to allow for Staff investigation. HAWC argued that bifurcation would accelerate investigation and approval of the DWGTF Loan which is time sensitive due to the narrowing construction season.

B. Staff

Staff recommended that the Commission find the DWGTF Loan consistent with the public good and approve the financing for an amount up to \$1,204,815 pursuant to RSA 369:1. In its recommendation, Staff relied on the DES letter filed on October 30, 2019, which was also included as part of HAWC's discovery responses. Staff specifically noted that DES agreed that the Project will provide numerous benefits: (1) increased reliability in the Company's water supply; (2) improved water quality by enabling HAWC to prioritize higher quality wells; (3) reduced system complexity by allowing the Company to reduce its number of active wells; and (4) enabled ability to address contamination and/or loss of water in private wells. Staff further noted that DES contended that HAWC's participation in the Project is necessary because of the Company's ability to wheel water through their system to serve Plaistow.

Staff calculated that HAWC's revenue requirement would increase an estimated 17.31 percent. That estimated increase, however, was not solely based on the cost of the financing, but inclusive of projected increases in the Company's operating expenses from Phase I and revenues from Plaistow.

Staff further determined that HAWC's capital structure would adjust 3 percent as a result of the financing, from 63 percent debt and 37 percent equity to 66 percent debt and 34 percent equity. While the capital structure remained a concern, Staff noted HAWC's shareholder's prior commitment, in Docket No. DW 18-138, to contribute at least \$750,000 to the Company between 2019 and 2021. Staff also noted that the Company intends to file a rate case once Phase I is complete, at which time HAWC's capital structure will be reviewed. As such, Staff considered the DWGTF Loan a routine financing and recommended approval.

Staff recommended that the Commission approve the motion to bifurcate, noting that it would promote the orderly and efficient conduct of this proceeding. Staff agreed with HAWC's

reasoning, and stated that the uncertainty of the proposed terms and conditions for the MSDC financing, including a lender, prevented it from completing its investigation. Staff agreed that the time-critical nature of the Project justifies bifurcation of the financing requests, and would allow the Commission to make a more prompt determination on the DWGTF Loan.

Staff, lastly, made its recommendation regarding HAWC's three additional requests. Staff recommended that the Commission determine: (1) approval is not necessary for the Company to receive the \$3,283,750 in DWGTF grant money, as the funds are not subject to repayment, thus not considered a financing under RSA 369:1; (2) a finding of prudence is not necessary in the context of this financing request, citing *Hampstead Area Water Company, Inc.*, Order No. 26,230 at 9 (March 29, 2019) ("the Commission's approval of the loan 'does not foreclose or limit our review in a future rate case of the prudence, use, and usefulness of any specific project directly or indirectly financed by this transaction'"); and (3) a simultaneous rate increase with the financing is inappropriate as it constitutes single-issue ratemaking.

III. COMMISSION ANALYSIS

RSA 369:1 states a utility "may, with the approval of the commission but not otherwise, issue and sell ... notes and other evidences of indebtedness payable more than 12 months after the date thereof for lawful corporate purposes." The Commission will conduct a "hearing or investigation as it may deem proper," then authorize sufficient financing "if in its judgment the issue of such securities upon the terms proposed is consistent with the public good." RSA 369:4. The Commission reviews, among other things, the amount of the proposed financing, the reasonableness of the terms and conditions, the proposed use of the proceeds, and the anticipated effect on customer rates. *Appeal of Easton*, 125 N.H. 205, 211-13 (1984).

The rigor of an *Easton* inquiry varies depending on the circumstances of the request. The Commission has previously noted, "certain financing related circumstances are routine, calling

for more limited Commission review of the purposes and impacts of the financing, while other requests may be at the opposite end of the spectrum, calling for vastly greater exploration of the intended uses and impacts of the proposed financing.” *New England Power Company*, Order No. 26,400 at 4 (August 31, 2020). “A routine request is one that will have no discernible impact on rates or deleterious effect on capitalization, and in which the funds are to enable numerous investments appropriate in the ordinary course of utility operations.” *Id.* A routine request calls for a more limited examination of whether the use of financing proceeds is in the public good without further review of possible alternative uses of the funds.” *Id.* at 5.

The Company seeks permission to receive a loan from the DWGTF in an amount up to \$1,204,815. The terms of the agreement include an amortization period of 25 years at an interest rate of 2.96 percent, with interest-only payments due for a term of six months after substantial completion of Phase I, followed by principal and interest payments. We note that the DWGTF is administered by DES and that the interest rate is lower than other financings. *See Hampstead Area Water Company, Inc.*, Order No. 26,230 at 1, 3 (March 29, 2019) (noting DES’s administration of the fund and interest rate of 3.38 percent for a similar loan); *see also Unutil Energy Systems, Inc.*, Order 26,391 (August 6, 2020) (approving a \$35 million financing at 5.25 percent).

Staff argued that the impact on rates and minimal change to HAWC’s capitalization structure deem this a routine financing. Consistent, however, with Order No. 26,230, we decline to consider the Company’s financing request as routine. In Order No. 26,230, we stated:

in consideration of the “Company’s past, present, and potential future financings, we must closely monitor the current and potential impact on HAWC’s capital structure. That requires the Commission to conduct a more comprehensive review of the public good. RSA 369:1 and :4.

Order No. 26,230 at 7. HAWC has not yet filed a full rate case, enabling the Commission to thoroughly examine the Company’s capital structure in light of recent financings, and HAWC’s

capitalization remains a focal point of concern. Consequently, we cannot find that this is a routine financing given our outstanding concerns highlighted in Order No. 26,230. We must accordingly conduct a more comprehensive review of the public good.

The Commission has noted that the “proper application of *Easton* is determined by the context of the facts and issues of the case.” Order No. 25,050 at 14. *Easton* requires that the Commission make a factual analysis when examining the public good of a financing. That analysis involves a balancing of consumer interests with HAWC’s right to manage its water business. In considering HAWC’s management decisions in this case, we must further consider that HAWC is requesting authority to borrow low-interest funds to cover its tax liability it will incur resulting from the CIAC it receives during Phase I construction of the Project. According to DES, HAWC’s participation in the Southern New Hampshire Regional Water Interconnection Project is critical, and will provide HAWC customers and potential new customers with a more reliable, safer water supply, and a reduction in system complexity. We acknowledge that the planning and decision-making process for the Project concluded before the tax law change in 2018, which resulted in an unanticipated additional \$1.1 million tax bill.

We recognize that receipt of CIAC is within the ordinary course of utility operation. We also acknowledge that the tax implications resulting from the 2017 Tax Cuts and Jobs Act has impacted all water utilities, prompting some to modify their tariffs. *See* Secretarial Letter, June 24, 2020 (*Hampstead Area Water Company, Inc.*, Docket No. DW 19-136) (approving tariff change “which would require a contributor of CIAC to pay an amount equal to the potential income tax liability associated with the CIAC”); *see also* Secretarial Letter, November 27, 2019 (*Pennichuck Water Works, Inc., Pennichuck East Utility, Inc., and Pittsfield Aqueduct Company, Inc.*, Docket No. DW 18-189) (approved “revisions would allow the Companies to recover tax costs, which occur when they receive CIAC property or payments”).

We find that although the DWGTF Loan may raise the rates of HAWC's existing customers at the outcome of the Company's rate case, and will increase HAWC's debt, this financing is nonetheless for the public good. The DWGTF Loan allows the Company to meet its mandatory income tax obligation for receipt of almost \$3.3 million of contributed, no-cost capital. HAWC, Staff, and DES have argued that the contributed capital will help promote the Company's duty to provide safe and adequate water service, pursuant to RSA 374:1. The financing for the tax is equivalent to buying the contributed capital at a steep discount.

We approve HAWC's request to secure the funds under the DWGTF loan program. Our approval of the DWGTF loan does not foreclose or limit our review in a future rate case of the prudence, use, and usefulness of any specific project directly or indirectly financed by this transaction. The Commission and Staff also retain the authority under RSA 374:4 to keep informed of HAWC's use of the financing independently and apart from any RSA 378:28 review.

We also approve HAWC's motion to bifurcate the financing requests. The Company argues, and Staff agrees, that separation of the financing requests will allow more time for investigation into the MSDC financing. Bifurcation of the financing requests would promote the orderly and efficient conduct of the proceeding. Accordingly, we grant the motion.

With respect to HAWC's additional requests, we agree with Staff's recommendation. We find that approval is not necessary for the Company to receive the \$3,283,750 in DWGTF grant money, as the funds are not subject to repayment, thus not subject to the financing requirements of RSA 369:1 and RSA 369:4. We also determine that a prudence finding is not required at this time, consistent with RSA 369:1 and RSA 369:4, and, will be conducted in HAWC's future rate proceeding. Lastly, we find, that consideration of a simultaneous rate

increase, requested by the Company but not fully argued, is inappropriate at this time and is better left to the full examination of HAWC's future rate case filing.

Based upon the foregoing, it is hereby

ORDERED NISI, that subject to the effective date below, the request of Hampstead Area Water Company, Inc., for approval of its proposed financing transaction of up to \$1,204,815 from the Drinking Water and Groundwater Trust Fund, on the terms described herein, is hereby APPROVED; and it is

FURTHER ORDERED, that Hampstead Area Water Company, Inc.'s requests for a prudence finding and simultaneous rate increase are hereby DENIED; and it is

FURTHER ORDERED, that Hampstead Area Water Company, Inc.'s motion to bifurcate its financing requests is hereby GRANTED; and it is

FURTHER ORDERED, that Hampstead Area Water Company, Inc., shall cause a copy of this order *nisi* to be published on its website within one business day, such publication to be documented by affidavit filed with the Commission on or before October 16, 2020; and it is

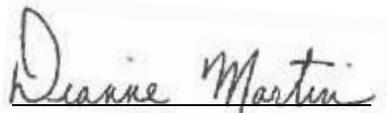
FURTHER ORDERED, that the Executive Director shall cause a copy of this order *nisi* to be published on the Commission's website within one business day; and it is

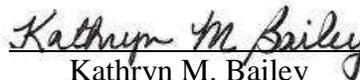
FURTHER ORDERED, that persons interested in responding to this order be notified that they may submit their comments or file a written request for a hearing, which states the reason and basis for a hearing no later than October 8, 2020, for the Commission's consideration; and it is

FURTHER ORDERED, that any person interested in responding to such comments or request for hearing shall do so no later than October 13, 2020; and it is

FURTHER ORDERED, that this order shall be effective October 19, 2020, unless Hampstead Area Water Company, Inc., fails to satisfy the publication obligation set forth above or the Commission provides otherwise in a supplemental order issued prior to the effective date.

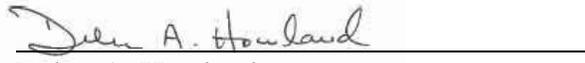
By order of the Public Utilities Commission of New Hampshire this twenty-eighth day of September, 2020.


Dianne Martin
Chairwoman


Kathryn M. Bailey
Commissioner


Michael S. Giaimo
Commissioner

Attested by:


Debra A. Howland
Executive Director

Service List - Docket Related

Docket#: 19-147

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