

STATE OF NEW HAMPSHIRE  
BEFORE THE  
NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION

*City of Nashua: Petition For Valuation Pursuant to RSA 38:9*

Docket No. DW 04-048

**REPLY TESTIMONY OF NASHUA MAYOR BERNARD STREETER,  
ALDERMAN BRIAN McCARTHY AND GEORGE E. SANSOUCY, P.E.**

1     **Q.   Please state your names and positions as they relate to this proceeding.**

2     A.   Bernard Streeter. Mayor for the City of Nashua.

3     A.   Brian S. McCarthy. I serve as a member of Nashua's Board of Alderman.

4     A.   George E. Sansoucy, P.E. My firm, George E. Sansoucy, P.E., LLC, has been  
5         engaged by the City of Nashua to advise it on matters concerning the City's  
6         proceeding to acquire the water utility assets of Pennichuck Water Works, Inc.

7     **Q.   Have you previously submitted testimony in this proceeding?**

8     A.   Bernard Streeter. Yes. On May 22, 2006, I provided reply testimony in this  
9         proceeding as a panel with David Rootovich, President of Nashua's Board of  
10        Aldermen, and Alderman Brian S. McCarthy.

11    A.   Brian S. McCarthy. Yes. On November 22, 2004, I provided testimony in  
12         support of Nashua's petition. On May 22, 2006, I also provided Reply Testimony  
13         as part of a panel with Mayor Streeter referenced above and as part of a second  
14         panel with Katherine Hersh and John Henderson, P.E., discussing Nashua's  
15         efforts to protect the Pennichuck Brook watershed.

16    A.   George E. Sansoucy, P.E. Yes. I have previously submitted the following  
17         testimony in this proceeding: On November 22, 2004, I provided testimony in  
18         support of Nashua's petition; on January 12, 2006, I provided testimony related to

1 the valuation of the Pennichuck Water Works, Inc. assets as well as public interest  
2 issues related to valuation including my analysis of customer savings that would  
3 result from Nashua's acquisition of the Pennichuck Water Works assets; and on  
4 May 22, 2006, I provided Reply Testimony responding to Pennichuck's valuation  
5 and public interest testimonies.

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

7 A. Our testimony today responds to the direct testimony of Mark A. Naylor, Randall  
8 S. Knepper and Amanda O. Noonan, members of the New Hampshire Public  
9 Utilities staff dated April 13, 2006. We believe that Staff's testimony unfairly  
10 criticized Nashua's Petition by adopting many of the Pennichuck arguments  
11 without conducting or presenting its own independent analysis. We further  
12 believe that Staff fundamentally misunderstood Nashua's proposal and failed to  
13 consider the benefits that the establishment of a municipally owned system would  
14 bring to the public interest, as well as key commitments Nashua has made in order  
15 to alleviate potential adverse impacts.

16

17 Because Staff adopted or relied heavily on Pennichuck's arguments, our May 22,  
18 2006 Reply testimony responding to Pennichuck already addresses many of the  
19 issues raised by staff. We urge the Commission to review our May 22, 2006  
20 Reply Testimony with this Testimony in evaluating our response to Staff's  
21 concerns.

22

23

1     **Q.     What is your general reaction to Staff's April 13, 2006 testimony?**

2     A.     Staff's April 13, 2006 testimony appears to be in part driven by the assumption  
3           that acquisition by Nashua will harm the public interest because of the impact that  
4           acquisition would have on existing customers outside of the Pennichuck Water  
5           Works core system. In addition, Staff appears to be concerned that Nashua's  
6           acquisition would cause Pennichuck to lose the ability to acquire small water  
7           systems throughout the State of New Hampshire that have a relatively high cost of  
8           operation per customer, and to operate those systems at either the Pennichuck  
9           Water Works core rates, or the rates charged by PEU or PAC.

10  
11          As set forth in our May 22, 2006 Reply Testimony and herein, we disagree with  
12          this position. Pennichuck has pursued a strategy of acquiring small high cost of  
13          service water systems that have resulted in the highest rates in the state for a  
14          system of its size.<sup>1</sup> We understand that, in addition to the rate increase recently  
15          approved in DW 04-056, the company now seeks an additional "effective increase  
16          of 43.11% for general metered customers."<sup>2</sup> These rate increases demonstrate  
17          that even in the absence of Nashua's petition, Pennichuck's ability to acquire and  
18          provide service to scattered, high cost satellite systems is limited by the  
19          inefficiencies it creates and its impact on rates.

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21          Were the Commission to adopt Pennichuck's and Staff's position in this  
22          proceeding, the net result would be to deny the Citizen of Nashua, Pennichuck's

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<sup>1</sup> See SMS Exhibit 8 Nashua Responses to Pennichuck Data Requests 5-9 & 5-10.

<sup>2</sup> NHPUC Order No. 24,646 (revised July 18, 2006), Page Two.

1 existing customers outside of Nashua and the State of New Hampshire, the  
2 opportunity to obtain local control of their water by establishing a municipally  
3 owned system as intended by RSA 38. The fact that Pennichuck Corp., has  
4 created a corporate structure that results in the subsidy of its regulated and  
5 unregulated subsidiaries should not be allowed to trump the legislative policy of  
6 local control established under RSA 38. This is particularly true in this case  
7 where Nashua will have the ability to operate the system at a lower cost to  
8 customers, focus on watershed protection and water conservation, and ultimately  
9 promote the establishment of a regional water district capable of addressing the  
10 region's water supply needs in an integrated manner.

11  
12 **Q. In his testimony Mr. Naylor identifies as the most important reason for his**  
13 **conclusion that the acquisition is not in the public interest the loss of PWW**  
14 **as a true regional water utility with a track record of cooperation on water**  
15 **supply and distribution issues. He argues that Pennichuck Water Work's,**  
16 **rather than Nashua, is the vehicle to achieve regionalization. Do you agree?**

17 A. No. There is no question that a regional approach which provides for better  
18 resource protection should be the future in New Hampshire; but the conclusion  
19 that Pennichuck Water Works is better able to achieve regionalization than  
20 Nashua makes no sense. The overwhelming majority of the water systems in  
21 southern New Hampshire, where the vast majority of the assets Nashua seeks to  
22 acquire are located, are owned by towns and cities with whom Nashua could join  
23 or partner with through intermunicipal agreements to advance regionalization. As



1 municipalities these cities and towns have greater planning capabilities and access  
2 to cheaper capital than Pennichuck Water Works.

3

4 Moreover, it is apparent from George E. Sansoucy, Exhibit 23, that beyond the  
5 core system consisting of Nashua and those municipalities hydraulically  
6 connected to the water treatment plant, Pennichuck's other systems are a series of  
7 isolated small community systems that have nothing to do with regionalization.

8 George E. Sansoucy, Exhibit 23 also demonstrates how this hodge podge of small  
9 community systems of Pennichuck and its sister companies interspersed among  
10 the municipal and district systems in southern New Hampshire, rather than being  
11 the vehicle for regionalization, are an impediment to it.

12

13 For example, consider PEU. According to Schedule S-2 to its 2005 Annual  
14 Report to the Commission, PEU required 448,533 million gallons, to serve its  
15 customers. Of this amount it produced itself 122,411 million gallons or about one-  
16 quarter of its needs. The remainder of 326,122 million gallons, approximately  
17 75% of its required water, PEU purchased from the surrounding **municipal**  
18 systems, Manchester, Derry, Hudson Hooksett and Raymond. PEU would not  
19 exist if it was unable to buy water from the from the municipal systems. These  
20 community systems like those of PWW should be municipally owned.

21

22 Pennichuck Corporation has developed a business plan which creates pockets of  
23 private ownership and private operation that stand in the way of the aggregation

1 of connected municipal water systems. Ultimately municipal entities are capable  
2 of forming larger regional partnerships and better able to achieve regional goals  
3 through tax exempt financing, resource conservation, sharing and development of  
4 operating and maintenance synergies beneficial to all members.

5  
6 For example, consider the formation of such authorities and districts as the  
7 Springfield Water and Sewer Commission, the Providence Rhode Island Water  
8 Supply Board, Massachusetts Metropolitan Water District, the Portland Water  
9 District and the City of New York to see the long term benefits of regionalization  
10 through a municipal entity.

11  
12 It is not enough to argue, as Mr. Naylor does, that municipal water suppliers “are  
13 not only not the answer to greater regional cooperation; many contribute to the  
14 lack of cooperation.”<sup>3</sup> Mr. Naylor ignores the fact that municipal enterprises that  
15 provide a greater benefit to the public at large, including citizens outside their  
16 political borders, are everywhere. In the area of municipal water utilities, the  
17 Manchester Water Works is an example of a municipally owned water utility that  
18 successfully serves some 167,000 customers in Auburn, Bedford, Derry,  
19 Goffstown, Hooksett and Londonderry as well as Manchester itself. Manchester  
20 Water Works uses 486 miles of water mains, owns and controls more than 8,000  
21 acres for water supply protection and has done so recently without rate increases,  
22 disruptions in service or water quality violations.<sup>4</sup>

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<sup>3</sup> Page 52 (emphasis in original).

<sup>4</sup> See MBS Exhibit 2 to the reply testimony of Nashua Mayor Bernard Streeter, et al, dated May 22, 2006.

1 In addition to Manchester, the City of Portsmouth provides water service from  
2 facilities located in Madbury using transmission mains that pass through  
3 Madbury, Dover, Durham to supply customers that are located in Newington,  
4 Portsmouth, Greenland, Rye and New Castle. Mr. Naylor's assertions also ignore  
5 other examples of inter-municipal cooperation resulting in greater service to the  
6 public in areas such as education, sewer services, solid waste management and  
7 fire and police protection.

8  
9 We also note that Pennichuck's efforts to portray itself as a regional utility acting  
10 in the best interest of its customers and the public conflict with its continued  
11 efforts to develop land within the watershed.<sup>5</sup> It is hard to imagine how the  
12 development of hundreds of acres of land within the watershed advances the  
13 cause of regionalization, even as the NHDES and Pennichuck's own consultants  
14 recommend that additional protections and conservation measures be provided.<sup>6</sup>

15  
16 Because Nashua will not operate under the investor owned model where the  
17 incentive is to maximize returns by maximizing the sale of water, Nashua will be  
18 better able to adopt conservation measures and engage in resource management.  
19 These practices will allow Nashua to achieve an optimum distribution and  
20 utilization of resources unavailable to Pennichuck and which clearly benefit the  
21 region.

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<sup>5</sup> See letter of Donald Ware urging the defeat of HB 1289. Exhibit 4 to Testimony of Katherine Hersh, et al.

<sup>6</sup> See generally, the May 22, 2006 Testimony of Katherine Hersh et al., and Alan Fuller, Ph.D.

1 **Q. Mr. Naylor states that the second most important reason Nashua's Petition is**  
2 **not in the public interest is because "the evidence clearly shows that the**  
3 **taking of PWW's assets will adversely effect rates in the other regulated**  
4 **water utilities owned by Pennichuck and will cause substantial harm to**  
5 **Pennichuck Water System Corporation".<sup>7</sup> Do you agree?**

6 A. No. Mr. Naylor made no independent analysis of the potential rate impact on  
7 PEU and PAC and no independent analysis of the impact on PWSC. Instead he  
8 accepted, uncritically, PWW's analysis contained in its supplemental response to  
9 Nashua Data Request 3-11. Pennichuck's claims adopted by Mr. Naylor are  
10 fundamentally flawed. See Reply Testimony of George E. Sansoucy and Glen C.  
11 Walker dated May 22, 2006 at page 25, et seq. Without performing any analysis  
12 of Pennichuck's claims, Mr. Naylor's assertions of harm to the other Pennichuck  
13 subsidiaries is merely an unsupported assumption or opinion and not entitled to  
14 any weight.

15  
16 Moreover, we believe PWW's claims contained in the response to Nashua 3-11  
17 suggest that Pennichuck's allocation agreement is flawed and creates subsidies  
18 that are not supportable. We are also troubled that PWSC has been included in  
19 this discussion. PWSC is unregulated for-profit enterprise and should not be  
20 supported by captive ratepayers served by regulated monopolies. Why should the  
21 ratepayers of Nashua provide a benefit to PWSC which makes it more profitable  
22 and in turn directly benefits the shareholders of Pennichuck Corp. Such a result is  
23 not the purpose of regulation.

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<sup>7</sup> Page 41.

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2     **Q.     Mr. Naylor has testified that his 3<sup>rd</sup> most important reason for reaching the**  
3           **conclusion that Nashua’s Petition is not in the public interest, is that**  
4           **Nashua’s proposal contains uncertainties and lacks evidence demonstrating**  
5           **that important functions such as customer service and billing and collections**  
6           **will be adequately addressed. Do you agree with this conclusion?**

7     A.    No. We particularly disagree with Mr. Naylor’s comments concerning the City’s  
8           use of Veolia Water as its contract operator and R.W. Beck as its oversight  
9           contractor. Public/private partnerships, such as this, are being increasingly  
10          utilized throughout the United States because of their ability to increase operating  
11          efficiencies, insure technical expertise and ensure water quality.<sup>8</sup> Even Donald  
12          Correll, the former President and CEO of Pennichuck Corp., in his testimony on  
13          behalf of Pennichuck before the United States House of Representatives  
14          Committee on Energy and Commerce on July 22, 2004,<sup>9</sup> recognized the benefits  
15          of public/private partnerships and their important role in reducing cost, freeing up  
16          capital for infrastructure replacement and avoiding significant rate adjustments  
17          while still meeting water quality standards. According to Mr. Correll, savings of  
18          as much as 40% can be achieved. And yet Staff still raises concerns that the  
19          benefits of these partnerships are uncertain.

20

21          In an effort to provide Staff with a better understanding of the public/private  
22          partnerships, Nashua and Veolia Water proposed that members of Staff travel to

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<sup>8</sup> SMS Exhibit 1, “An Evaluation of Public/private Partnerships for Water and Waste Water Systems”  
prepared by the Water Partnership Council, dated June, 2005.

<sup>9</sup> SMS Exhibit 2

1 Indianapolis, Indiana to observe the largest public/private partnership in the  
2 country in operation and to meet directly with both City and Veolia officials to  
3 discuss its operation and management of the Indianapolis water system using the  
4 public/private partnership. It is unfortunate that Staff did not pursue this  
5 opportunity and instead appears to have relied on the unsubstantiated newspaper  
6 articles produced by Pennichuck. As set forth in the January 12 and May 22  
7 testimony of Philip Ashcroft et al,<sup>10</sup> Veolia's operation of the Indianapolis Water  
8 system has resulted in substantial benefits and improvements to the water system  
9 that the prior investor-owned utility, NiSource, failed to provide. Veolia's  
10 operation and management of the system has resulted in lower operating costs in  
11 2006 than when it bought the investor-owned system from NiSource and  
12 contracted operations to Veolia Water in 2002.<sup>11</sup> Furthermore, any concern about  
13 uncertainties in the integration of operation and oversight could readily be cured  
14 with a condition of approval adopted by the Commission. Staff, however, has not  
15 articulated what its real concern is nor suggested what would satisfy it.

16  
17 Finally, the testimony of Amanda Noonan concerning customer service and  
18 billing is simply wrong as set forth in the May 22, Reply Testimony of Nashua's  
19 Chief Financial Officer Carol Anderson et al., at Pages 4 (lines 21-23) and 5 (line  
20 1-8). It was Ms. Noonan's testimony that Nashua would have only 4 full time  
21 staff available for customer service, of which 2 were Veolia employees who

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<sup>10</sup> See, e.g., January 12, 2006 *Testimony of Philip Ashcroft et al*, Exhibit A containing Volume III, Appendix B, Part 1 of Veolia Water's technical proposal to the City of Nashua; May 22, 2006 *Reply Testimony of Philip Ashcroft et al.*, Pages 6-8 & Exhibits B through E.

<sup>11</sup> SMS Exhibit 3, Public Works Financing, June 2006, Volume 206, PP 1 and 2

1 would handle only water system operating issues. However, the 2 new City  
2 employees would be added to the current 6 employees in the City Treasurer/Tax  
3 Collection Department and all 8 employees would be cross-trained to deal with  
4 water issues as well as property tax and sewer bills. Including the 2 Veolia  
5 employees the total Nashua customer service personnel will actually exceed the 9  
6 full time customer service staff of PWW.

7  
8 Moreover, Ms. Noonan's testimony does not address the substantial meter reading  
9 errors and billing problems discovered by the City described in the testimony of  
10 Carol Anderson et al in their testimony at page 4, that resulted from data provided  
11 by Pennichuck. These problems have resulted in wastewater fee refunds by  
12 Nashua and additional employee expenses. The full extent of the current problem  
13 has not yet been determined.

14  
15 **Q. Mr. Naylor is also critical of what he asserts will be a reduction of the work**  
16 **force under Nashua's ownership to approximately two-thirds of PWW's**  
17 **current level. He asserts that because of the reduction there will be a**  
18 **degradation of customer service. Do you agree?**

19 A. No. This criticism appears to be the result of a misunderstanding of the role of  
20 Veolia Water will perform. In the first instance, Nashua and Veolia do not  
21 propose that the number of line employees will be significantly reduced, if at all.  
22 What will be eliminated is the relatively high management and administrative  
23 costs resulting from PWW's ownership. These management and administrative

1 functions will be absorbed by Veolia Water. That is one of the reasons the public-  
2 private partnership can reduce cost. There is no benefit in that model to creating a  
3 large administrative staff as exists in the IOU model where the cost is simply  
4 passed through to ratepayers.

5 **Q. Mr. Naylor says that the 4<sup>th</sup> most important reason for his determination**  
6 **that Nashua's acquisition is not in the public interest is that acquisitions of**  
7 **all troubled water systems by Pennichuck and its affiliates are not likely to**  
8 **continue if PWW ceases to exist.<sup>12</sup> What is your reaction to Mr. Naylor's**  
9 **testimony?**

10 A. Mr. Naylor's testimony ignores Nashua's intent to consider such acquisitions on a  
11 case by case basis as set forth in its July 29, 2005 Response to Staff Data Request  
12 2-6. (Exhibit MAN-17) This intent has been made clear and was again reiterated  
13 in the Nashua's May 22, 2006 Reply Testimony. See *Testimony of Bernard*  
14 *Streeter et al*, Pages 17-20 & 23; *Testimony of George E. Sansoucy, P.E. et al.*,  
15 Pages 23-24.

16  
17 Mr. Naylor's testimony also ignores the many municipal water systems that  
18 provide water to surrounding communities, including Manchester Water Works  
19 and the City of Portsmouth described above. There are many examples where  
20 municipal systems have extended service beyond their municipal boundaries for  
21 the common good and in the assertion that Nashua would approach the operation  
22 of its water system and the potential acquisition of a troubled water system purely  
23 in terms of its own bottom line and self interest is cynical and unsupported.

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<sup>12</sup> Page 42.



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Nashua’s Petition in this proceeding in which it sought to acquire the assets of PEU and PAC in addition to PWW, in itself is an example of a municipality looking beyond its own borders in order to provide a greater service to the public. We have already pointed out how municipalities collaborate, not only in providing water services but also in such other areas as education, sewer, solid waste and fire and police protection. In addition, the evidence is clear that municipalities can provide service at lower cost than investor owned utilities like Pennichuck. See New Hampshire Department of Environmental Services 2004 Water Rate Survey as analyzed in the New Hampshire Business Review, Volume 27, No. 9, April 29-May 12, 2005.<sup>13</sup>

We certainly understand that under the existing regulatory structure Pennichuck Water Works has an incentive to expand its franchise outside of Nashua by acquiring inefficient, troubled water systems regardless of their location and whether they contribute disproportionately to the overall cost of service. An investor owned regulated utility has an automatic right to recover its operating costs based on the system it owns, even if that system is a hodge podge of disconnected systems scattered throughout the State. Moreover, without growth and regardless of the quality of the growth, a regulated utility can not increase its revenues; and growth for the sake of growth, therefore becomes its goal regardless of cost.

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<sup>13</sup> SMS Exhibit 4

1 As a consequence, while Pennichuck's focus is on profit from any region or area  
2 of the State, Nashua's focus will be in the areas it serves and its desire to protect  
3 and serve the needs of the lower Merrimack River region. We think this approach  
4 represents true regionalism.

5  
6 The role of Veolia Water, in the discussion of troubled water systems should not  
7 be overlooked. Veolia Water is one of the largest contract operators in the world  
8 and operates systems as large as Indianapolis, Indiana and as small as any of the  
9 Pennichuck satellite systems. Veolia Water would be an alternative to  
10 Pennichuck available to Staff and the owners of the troubled systems. And even  
11 if Veolia is not the answer, we believe other utilities will fill the role Staff  
12 believes PWW provides. Even now PWW is not the only NH utility acquiring  
13 troubled systems.<sup>14</sup>

14  
15 Finally, we think it is important to point out that Mr. Naylor's testimony  
16 concerning the role of Pennichuck and troubled systems overstates Pennichuck's  
17 role. Pennichuck does not acquire every troubled system in the State of New  
18 Hampshire. It did not acquire, for example, Gunstock Glen, as noted in the  
19 Rebuttal Testimony of Bonalyn J. Hartley dated February 23, 2005 filed in  
20 Pennichuck Water Works recent rate case (DW 04-056), nor has it acquired a  
21 system in East Conway from Fryeburg Water.

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<sup>14</sup> SMS Exhibit 5, Staff Response to Nashua 6-46

1 In her recent deposition (not yet been transcribed) Ms. Hartley testified that the  
2 company had not completed the acquisition of other troubled systems after  
3 reviewing their costs of operation and other factors. Apparently Pennichuck  
4 applies a similar case by case analysis to that which the City proposes. While it is  
5 probably unlikely that the City would pursue acquiring systems such as those in  
6 Gilford or Conway, it would do so in and adjacent to its existing franchises.

7  
8 **Q. Mr. Naylor's testimony states that Nashua's projection that it will have a**  
9 **lower cost of service is speculative considering that Nashua's rate projections**  
10 **are based on the City's estimate of value. In support of this conclusion, Mr.**  
11 **Naylor states that Nashua has underestimated certain costs and as a result**  
12 **"based solely on Nashua's estimate of the value of PWW's assets it appears**  
13 **that Nashua would have a slightly reduced costs of service."**<sup>15</sup> **What is your**  
14 **reaction to this testimony?**

15 **A.** We are troubled that the Staff has given any weight to Pennichuck's valuation  
16 testimony. We hoped that Staff would take into account not only that Pennichuck  
17 Water Works proposed value substantially exceeds what it can return to investors  
18 but also more than doubles the market based enterprise value of its parent,  
19 Pennichuck Corporation.<sup>16</sup>

20  
21 Mr. Naylor simply notes the truism that the question of actual savings will remain  
22 uncertain until such time as a value is set by the Commission. It is unfortunate

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<sup>15</sup> Page 42.

<sup>16</sup> SMS Exhibit 6 Smart Money.com

1 because we firmly believe that any reasonable determination of value in this  
2 proceeding would demonstrate Nashua's ability to provide service to customers at  
3 lower cost than Pennichuck and demonstrate that Nashua's petition is in the  
4 public interest.

5  
6 **Q. Do you accept Mr. Naylor's conclusion that Nashua understated its costs?**

7 A. No. Mr. Naylor has accepted Donald Ware's February 27, 2006 testimony in  
8 which he asserts that Nashua has understated unplanned maintenance, the cost of  
9 purchased water, the cost of fuel and electricity and cost related to the dig safe  
10 program. Mr. Naylor's concerns, however, reflect a misunderstanding of how  
11 unplanned maintenance will be addressed in Nashua's Operations Maintenance  
12 and Management Agreement (OM&M) with Veolia Water.<sup>17</sup>

13  
14 Many of the items which Pennichuck Water Works refers to as unplanned  
15 maintenance are included in the category OM&M Services set forth in Appendix  
16 D to the Agreement. OM&M Services are included in the Annual Fee Nashua  
17 will pay to Veolia Water. To the extent that there are planned or unplanned  
18 maintenance items not included in the Annual Fee, they are included in Appendix  
19 H as Renewal, Repair and Replacement Maintenance. Nashua has budgeted  
20 \$185,000.00 for these services plus a contingency of \$500,000.00 for unplanned  
21 repairs. In the event unplanned maintenance exceeds this amount Nashua is  
22 funding a reserve account annually in excess of \$700,000.00. See GES Exhibits  
23 4,5 and 6.

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<sup>17</sup> See January 12, 2006 Testimony of Philip Ashcroft et al.

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As a result, Pennichuck’s and Staff’s analysis is based on the incorrect assumption that items such as “unplanned maintenance” has not been accounted for under Nashua’ projections when in fact those items have been included in the Annual Fee for OM&M Services, RRRM services, and in reserve accounts as set forth in GES Exhibits 4, 5 & 6.

The suggestion that Nashua understated the cost of purchased water and fuel and electricity for the pumping plant is more troubling. In Schedule F-48 to Pennichuck Water Works Annual Report to the Commission for the year ended December 31, 2004, the most recent report available to Nashua at the time its valuation and revenue requirements analysis were performed, there is no entry for purchased water (Account 602) and the cost for fuel or power purchased (Account 623) was \$556,441.00. Nashua was aware that Pennichuck purchased water and therefore budgeted \$100,000.00 for that cost and 550,000.00 for power and fuel. In Schedule F-48 for the Annual Report for the year ended December 31, 2005, which was relied upon by Staff although not available to Nashua or the public at the time of Nashua’s testimony, the cost of purchased water (Line 602) was \$182,125.00, a totally new entry and a 100% increase from 2004. Fuel or power purchased for pumping (Line 623) increased \$413,737.00 from 2004 to a total of \$970,178.00.

1        These costs, which Nashua is criticized for understating were improperly  
2        accounted for in the 2004 annual report which was the most recent report  
3        available to Nashua and on which it assumed it could rely. Pennichuck, in 2005,  
4        changed its accounting, criticized Nashua for understating its costs and then  
5        provided only Staff a copy of the new schedule so that Staff could adopt its  
6        criticism of Nashua.

7  
8        Nashua has always anticipated that adjustments to its revenue requirements  
9        analysis would be necessary and these adjustments will be made for its final  
10       presentation to the Commission. We note, however, that these adjustments in the  
11       overall revenue requirements analysis are minor and will have a limited impact on  
12       the savings that will be achieved by ratepayers if Nashua is permitted to acquire  
13       the assets of Pennichuck Water Works. They are well within the contingency and  
14       reserves established in Nashua's pro forma budget. See GES Exhibits 4,5 and 6.

15  
16    **Q.    The final reason given by Mr. Naylor for his conclusion that Nashua's**  
17       **acquisition was not in the public interest was that he was concerned that**  
18       **Nashua's attitude toward Pennichuck Water Work's acquisition of its**  
19       **satellite systems would compromise the level of service and capital**  
20       **improvements those systems would receive under Nashua's ownership.<sup>18</sup>**  
21       **Should he be concerned?**

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<sup>18</sup> Page 44.

1 A. Absolutely not. Nashua has consistently indicated that it will provide service to  
2 the satellite systems at the same core rates as it charges rate-payers of Nashua.<sup>19</sup>  
3 Nashua's commitment is unequivocal. We are disappointed that Staff does not  
4 fully understand or recognize that commitment.

5  
6 There is no doubt that Nashua believes that its ratepayers have in the past and  
7 continue to subsidize acquisitions by not only by PWW, but also by PEU and  
8 PAC, in addition to PWSC's service operations. Nashua cannot, however, turn  
9 back time. The satellite systems exist and Nashua stands behind the principle of  
10 providing the same level of service at the same rates regardless of location.  
11 Nashua does not believe, however, that its ratepayers, because of Pennichuck's  
12 corporate structure, should be required to subsidize, **ad infinitum**, Pennichuck's  
13 growth regardless of where it occurs. Mr. Naylor fails to recognize this  
14 distinction.

15  
16 Nashua has made a number of commitments that will benefit the public interest  
17 and ensure that the interest of customers located outside of Nashua are protected  
18 and treated fairly in all respects which have been ignored by Mr. Naylor. For  
19 example, Nashua has committed to operate its water system according to the  
20 terms of its Water Ordinance in a manner that treats all customers equally. In  
21 addition, to the extent that Nashua serves customers outside of its borders it has  
22 agreed and committed to the principle that the terms and conditions of its service,

---

<sup>19</sup> See e.g. May 22, 2006 Reply Testimony of Mayor Streeter et al, Exhibits 4 & 5; Nashua's March 20, 2006 Response to Staff Data Request 4-33

1 i.e., its Water Ordinance will be continue to subject to the jurisdiction of the  
2 Commission under RSA 362:4 and RSA 374. See MBS Exhibit 3.

3

4 Finally, Nashua has committed, as we stated above, to provide service to all  
5 satellite customers at core rates, notwithstanding its authority to charge satellite  
6 customers higher rates. Nashua fully expects that the Commission, in its  
7 discretion, will make these commitments into appropriate binding conditions upon  
8 its acquisition of the water system. We note that as recently as December 9, 2005,  
9 the Commission stated in Order No. 24,562 that pursuant to RSA 362:4, III-a  
10 (a)(1), a municipal corporation providing water service “must provide the same  
11 quantity and quality of water or level of water service to customers outside” its  
12 borders.

13

14 We are troubled that Mr. Naylor, in light of the many commitments made by  
15 Nashua, would express such concerns. He has either misunderstood the level of  
16 Nashua’s commitment to the customers of the satellite systems or he has chosen  
17 to ignore them because they do not support his conclusion. In either case,  
18 however, any concern he has with respect to rates, customer service, maintenance  
19 and future capital improvements in the satellite systems is misplaced.

20

21 **Q. In his testimony Mr. Naylor discusses the assertion by Nashua that**  
22 **Pennichuck has not been a good steward of the watershed and concludes that**  
23 **there is not any “objective evidence” which identifies instances of harm or**



1           **mismanagement by Pennichuck resulting in degradation of water quality or**  
2           **increased treatment costs? What is your reaction to this testimony?**

3       A.     The Reply Testimony of Katherine Hersh, Brian McCarthy and John Henderson,  
4           P.E. and the Reply Testimony of Allan Fuller, PHD is replete with objective  
5           evidence of mismanagement of the watershed by Pennichuck, which has resulted  
6           in degradation of water quality or increased cost. We hope this testimony will  
7           change Mr. Naylor's opinion.

8  
9           For example, in the 1998 Draft Watershed Management Plan, prepared by Eileen  
10          Pannetier of Comprehensive Environmental, Inc., it was noted that sampling data  
11          showed excess levels of phosphorus in most of the ponds. The report continued:  
12          "These excess levels were identified considering the detention the chain ponds  
13          provide to one another in series. **This is the result of the overwhelming**  
14          **detriment of development which has increased nutrient loadings into the**  
15          **ponds reducing both their capacity and detention benefit.** Based on the  
16          identified phosphorus levels in the ponds, actions need to be taken to reduce the  
17          existing loadings into the system and to minimize additional loadings from future  
18          development."<sup>20</sup>

19  
20          To deal with the problems she identified Ms. Pannetier recommended that  
21          Pennichuck require a 300' setback/buffer from all tributaries to the chain pond  
22          system, including the pond systems themselves and work with local planning  
23          departments and conservation commissions to incorporate a 300' buffer in local

---

<sup>20</sup> Exhibit 6 to Reply Testimony of Katherine Hersh, et al, page 8-1 (emphasis added).

1 subdivision and planning regulations. Although Pennichuck could have  
2 petitioned NHDES to under RSA 485:23, 24 to adopt the setbacks recommended  
3 by its consultant, it did not do so and instead publicly opposed the Water Supply  
4 District adopted by the Nashua Board of Alderman and more recently opposed  
5 House Bill 1289 before the New Hampshire Senate in April, 2006. House Bill  
6 1289 would have implemented, on a permanent statutory basis, the 1998 final  
7 recommendation for setbacks and buffers of 400' and 200' for the surface waters  
8 and tributaries. House Bill 1289 had strong support from NHDES. In his April  
9 18, 2006 letter of support, Commissioner Michael Nolan noted that DES  
10 considers any development in a water supply watershed to represent a potential  
11 threat to the quality of the water supply source and went on to state that DES, the  
12 United States Environmental Protection Agency and the Water Supply Profession  
13 "do not consider treatment alone to be the preferred approach to insuring safe  
14 drinking water. The preferred approach, the so-called multiple-barrier approach,  
15 includes source protection as a key component. . . . Source Protection consists of  
16 maintaining a water supply/watershed in its natural state."<sup>21</sup> By contrast, PWW  
17 opposed HB 1289 because of the impact on its ability to develop the rest of its  
18 watershed land , calling the legislation "a regulatory taking".  
19

20 **Q. Are there other examples of objective evidence of the harm to the watershed**  
21 **caused by Pennichuck?**

22 A. Yes. The final 1998 Watershed Management Plan, prepared by CEI, concluded  
23 that "the existing Pennichuck owned land should be conserved to minimize the

---

<sup>21</sup> Exhibit 4 to Reply Testimony of Katherine Hersh, et al.

1 impacts of urbanization and to provide adequate buffer to the chain ponds and  
2 their tributaries.”<sup>22</sup> The Report further stated that a more significant reduction in  
3 pollutant loading to the supply pond chain can be achieved “if the amount of  
4 conservation land owned by Pennichuck Water Works or others were larger”.<sup>23</sup>  
5 The plan further noted that the number of regulated drinking water contaminants  
6 in the ponds had increased from less than 20 to more than 100 in the 10 years  
7 between 1988 and 1998 and concluded that “Raw water, bacteria and nutrients are  
8 troublesome and may lead to increased [treatment] cost in the future. Even more  
9 critical is the increasing inability to store water in the watershed. Urbanization  
10 will continue to reduce the available water supply.”<sup>24</sup>

11  
12 As noted in the Reply Testimony of Katherine Hersh, et al, by 2003 the conditions  
13 noted by CEI in the supply pond system had become so bad that Pennichuck  
14 undertook a new study to address water quality problems which were adversely  
15 impacting their ability to treat and produce high quality potable water. The water  
16 quality problems identified by Pennichuck were classic conditions resulting from  
17 development of the watershed resulting from development of the watershed and  
18 resulted in a significant investment in baffles, weirs and aeration equipment to  
19 control the flow of pollutants through the ponds system to minimize their adverse  
20 impacts on water quality.

---

<sup>22</sup> Exhibit EP-3, Section 6.4, page 6-15

<sup>23</sup> Exhibit EP-3, Section 2.6, pages 2-5

<sup>24</sup> Exhibit EP-3, Section 2.6, pages 3-5

1 To illustrate the importance of this issue, as referenced in the Reply Testimony of  
2 Katherine Hersh et al., Nashua has prepared two maps showing the land held by  
3 the Pennichuck Water Works in 1980 compared to what it holds today. See SMS  
4 Exhibit 8. Most troubling is the fact that substantial sales and development of the  
5 Pennichuck Corporation's water supply protection land continued to take place  
6 even after the Pennichuck officials, including its CEO, had fully reviewed and  
7 prepared in the 1998 draft and final Watershed Management Plans. The fact that  
8 Pennichuck is apparently unwilling to give up on its real estate development  
9 activities even when its own consultants recommend that do so.

10

11 Also included in SMS Exhibit 8 is a map documenting the location of the  
12 properties acquired by the City of Nashua for protection of the Pennichuck Brook  
13 watershed, also referenced in the May 22, 2006 *Reply Testimony of Katherine*  
14 *Hersh et al.* This second map shows Nashua commitment to protect the  
15 Pennichuck Brook water supply through land conservation and has even  
16 purchased Pennichuck lands in order to protect the watershed from development.

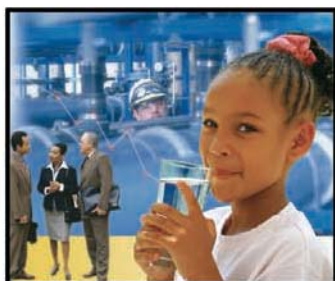
17

18 **Q. What concerns do you have for the future of the watershed?**

19 A. As noted in the *Reply Testimony of Katherine Hersh, et al.*, because of the increase  
20 in development in the watershed there has been an increase in storm water flows  
21 and intensity and a reduction in the amount rainfall that is recharged to the ground  
22 water. The increase in storm water flows has lead to greater deposition of silts  
23 and contaminants in the chain pond system which has decreased its storage

1 capacity and contamination simulation capacity. The reduction in the amount of  
2 rainfall that is recharged to the ground water has reduced the yield capacity of the  
3 chain pond system. A loss of capacity or safe yield is potentially more  
4 problematic than the deterioration in raw water quality.

5  
6 Ultimately, water can be treated at additional cost to address deteriorating raw  
7 water quality. On the other hand, a loss of capacity or safe yield due development  
8 may be impossible to reverse. We worry that Pennichuck's stated goal to develop  
9 the remaining 500 acres in the watershed held by Southwood Corporation may be  
10 the straw that breaks the camel's back.



*An Evaluation of  
Public-Private  
Partnerships for  
Water and  
Wastewater  
Systems*

*June 2005*



SMS EXHIBIT 1





## ACKNOWLEDGEMENTS

This report was prepared by the staff of the Water Partnership Council, a non-profit organization established in 2001 by the leading providers of operational services for water and wastewater systems in the United States. The Council seeks to partner with citizens, local governments, and organizations committed to strengthening the U.S. water and wastewater infrastructure. The Water Partnership Council is dedicated to helping communities and companies in America meet their water and wastewater needs in the safest, most environmentally sound, most cost-effective manner possible.

Members of the Council are American Water, OMI, Inc., Severn Trent Services, Southwest Water Company Services Group, United Water, and Veolia Water North America.

To prepare this report, Water Partnership Council staff conducted more than 30 interviews between December 2004 and May 2005. We thank all of the public officials, industry experts, and other stakeholders who shared their experiences with us. We note particularly *Public Works Financing*, which provided us with industry statistics, as well as those communities that shared their partnership experiences.

### Participating communities

Bexar Metropolitan Water District  
- San Antonio, Texas  
Boyertown, Pennsylvania  
Burkburnett, Texas  
Burbank, California  
Clarksville, Indiana  
Coos Bay, Oregon  
Dade City, Florida  
Dedham - Westwood, Massachusetts  
Dos Palos, California  
Edwardsville, Illinois  
Fayetteville, Arkansas  
Freeport, Texas  
Fulton County, Georgia  
Glynn County, Georgia  
Indianapolis, Indiana  
Jackson, Mississippi  
Jacksonville, Florida  
Keystone, South Dakota  
Lathrop, California  
Leominster, Massachusetts  
Milwaukee, Wisconsin  
Moore, Oklahoma  
New Bedford, Massachusetts  
Reidsville, North Carolina  
Rialto, California  
Rio Rancho, New Mexico  
Tri-Cities North Regional Water Authority, Ohio  
Waterbury, Connecticut  
West Basin Municipal Water District  
- El Segundo, California  
Woonsocket, Rhode Island  
Yukon, Oklahoma





## SMS EXHIBIT 1

## SMS EXHIBIT 1

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## SMS EXHIBIT 1

### EXECUTIVE SUMMARY

The use of public-private partnerships for water and wastewater services in the United States has been both praised and challenged. However, to date, neither point of view has been supported by statistical data. This report presents the results of 31 interviews with representatives of public entities that contract the day-to-day management, operation, and maintenance of their water and/or wastewater facilities to a private partner—in whole or in part. The facilities serve populations ranging from 4,000 to 1.2 million. The total population covered by the surveyed partnerships is 4.7 million.



#### *Satisfaction with partnerships and partners is high:*

- 50 percent of respondents rate overall satisfaction with the partnership as “extremely satisfied,” the highest possible ranking. No respondents rate overall satisfaction anything less than “satisfied.”
- 86 percent of municipality respondents that had a prior partnership awarded the contract to the incumbent.
- 50 percent of respondents rate the technical competence of their private partner as “outstanding.”
- 57 percent of respondents rate the quality of communication with their private partner as “outstanding.” No respondents rate the quality of communication anything less than “satisfactory.”

#### *Impact on the environment, customers, and municipalities is positive:*

- 74 percent of respondents rate regulatory compliance as better under the partnership than prior to the partnership.
- 93 percent of respondents note that customer complaints decreased or remained the same under the partnership.
- 92 percent of the municipalities that projected cost savings before entering the partnership achieved the projected savings. The other 8 percent are too early in the contract term to evaluate.
- 93 percent of respondents note that their private partners proactively participate in community activities above and beyond what is required in their contract.

#### *Employees are generally satisfied:*

- 21 percent of respondents rate employee satisfaction as “extremely satisfied.” All respondents rate employee satisfaction as at least “satisfied.”
- None of the respondents report an increase in employee grievances under the partnership. In fact, 64 percent report a decrease.
- 93 percent of respondents note that involuntary employee turnover either declined or remained the same under the partnership.
- 93 percent of respondents state that employees have more educational and training opportunities and more professional growth opportunities with their private partners than they did with the municipality.
- 87 percent of respondents report that employee salaries increased or remained the same under the partnership.
- 60 percent of respondents note that employee benefits increased or remained the same under the partnership.

The following sections of the report present detailed findings on general satisfaction with partnerships and the impact of partnerships on the environment, the customers, the municipality, and the employees.

## SMS EXHIBIT 1

## SMS EXHIBIT 1

*This report begins with an overview of public-private partnerships, followed by a discussion of the respondents' general satisfaction with partnerships and their private partners. It then details the impacts of partnerships on customers, municipalities, employees, and the environment.*

*It is based on the results of a survey of representatives of public entities engaged in public-private partnerships. The Water Partnership Council believes this survey to be the first ever of U.S. municipalities and water districts that participate in public-private partnerships.*

### OVERVIEW OF PUBLIC-PRIVATE PARTNERSHIPS

The public entities that responded to this survey contract the day-to-day management, operation, and maintenance of their water or wastewater facilities to a private partner—in whole or in part. Some of the public entities also contract customer service functions and/or had their facilities designed and built by their private partner. Contracts typically range from 3 to 20 years.

A partnership is not privatization. Although the terms “public-private partnership” and “privatization” often are used interchangeably, they are not the same. Privatization involves the sale or transfer of ownership of public assets to the private sector. In sharp contrast, under all public-private partnerships, the public partner owns the assets, controls the management of the assets, and establishes user rates. The private partner operates and maintains the facility under a contract with the public partner.



A municipality will enter into a partnership to:

- **Ensure Water Quality and Achieve Regulatory Compliance.** A private partner's ability to secure new contracts rests to a significant degree on how well it manages its existing contracts. Therefore, private partners have powerful incentives to comply with federal and state water and wastewater quality standards. The private partner works closely with environmental stakeholders and regulators to operate the systems in compliance with stringent regulations at all times. The private partner takes responsibility for regulatory compliance through a service agreement with specific performance standards. In cases of permit violation, payment of penalties is generally the responsibility of the private partner, not the public entity.
- **Ensure Technical Expertise.** Water and wastewater operations are just a small part of the daily business a municipality must conduct. As a result, some municipalities, small and large alike, have trouble recruiting and retaining qualified water and wastewater plant operators and keeping abreast of new technologies and techniques. In contrast, private partners focus their businesses on the operation and maintenance of these facilities. This experience can translate into more efficiently run plants from a cost and regulatory perspective.
- **Increase Operating Efficiencies.** A public-private partnership often results in increased operating efficiencies and annual operating cost savings to the municipality, sometimes allowing municipalities to avoid or mitigate increases in customer water rates.

More than 2,800 partnerships exist today, and this number is growing. Last year, *Public Works Financing*<sup>1</sup>, with additional data collected by the Water Partnership Council, tracked more than 1,200 municipal clients with partnerships in 2004. This was a 7 percent increase over 2003. And, this number represents only eight<sup>2</sup> of the firms that participate in public-private partnerships.

<sup>1</sup> *Public Works Financing*, March 2005, Volume 192.

<sup>2</sup> Companies that reported numbers include: Alliance Water, American Water, Aquarion Operating Services, OMI Inc., Severn Trent Services, Southwest Water Services Group, United Water, and Veolia Water North America.

## SURVEY METHODOLOGY AND POPULATION

The survey was conducted by the Water Partnership Council staff. The Council staff performed telephone interviews from a standard questionnaire that included open- and closed-ended questions. Closed-ended questions asked for before-and-after comparisons. For example, “Is environmental stewardship better, equal, or worse today as compared to before the partnership?” A copy of the questionnaire is contained in Appendix A.

Council staff probed for additional information on the closed-ended questions. Member companies provided Council staff with the contact information for potential municipal respondents. The survey had a response rate of slightly more than 50 percent.

The survey instrument is comprehensive, and questioned public officials from both large and small communities. Each respondent’s facility is presently managed within a public-private partnership. Over time, the Council hopes that this survey will grow in scope and depth. It is a first effort at establishing objective information on partnerships and their strengths and weaknesses. As a body, the Council is committed to the continued improvement and efficacy of public-private partnerships as a mechanism for providing efficient, high-quality water services.

More than 30 municipal representatives participated in the telephone survey. Not everyone was able to answer every question because of his/her varied range of experience with the partnership. Response rates on individual questions ranged from a low of 11 responses to a high of 31.

The respondents represent partnerships that serve a mix of populations. Populations range from 4,000 to 1.2 million with an average population of approximately 143,000. The total population served by the partnerships is 4.7 million.

The survey covers operations of water and wastewater facilities:

- Twelve respondents partner for both water and wastewater operations
- Four respondents partner for water operations only
- Fourteen respondents partner for wastewater operations only
- One respondent partners only for the municipality’s collection and distribution system

In total, the survey represents 27 water plants and 27 wastewater plants. Some clients have more than one water or wastewater plant under contract.

The water and wastewater plants vary in size. The 27 water plants range in size from 0.5 million gallons per day (mgd) to 100 mgd. The average size of the water plants in the survey is 16.2 mgd. The 27 wastewater plants range in size from 0.75 mgd to 100 mgd. The average size of the wastewater plants in the survey is 13.7 mgd.

Contracts range from 3 to 20 years with potential extensions ranging from 0 to 10 years. The average contract length is 9.2 years, and the average potential extension is 4.8 years, when an option to extend exists. The contracts have been in effect for an average of 3.6 years and, not including extensions, an average of 6.2 years remains on these contracts.

The following sections first present data relating to overall satisfaction with partnerships and then detail the impact of partnerships on customers, municipalities, employees, and the environment.





## GENERAL PARTNERSHIP SATISFACTION

Municipal officials see real and tangible benefits from partnerships. One of the most important benefits that municipal officials cite is having access to greater expertise than they would otherwise.

This expertise provides additional benefits. It alleviates one concern of municipalities—the municipality does not have to worry about the plant. Many respondents point out they do not think about the plants on a daily basis because they believe that their partner is acting in the municipality’s best interest. This frees up municipality staff time and resources.

Respondents note other benefits, including:

- Handling employee relations and benefits
- Providing the same level of service at a lower cost
- Protecting the operations budget
- Assuming liability and risk for environmental compliance
- Recruiting and retaining operators
- Purchasing materials in an expedited manner

These benefits translate into high levels of municipal satisfaction with the **partnerships in** general, and their partners specifically. Respondents rated their **satisfaction** with the partnership on a scale from one to five—with five being “extremely satisfied,” three being “satisfied,” and one being “not satisfied at all.” The average response was a 4.5, with 50 percent of respondents giving a 5; 47 percent, a 4; and 3 percent, a 3. Participants state that their satisfaction was based on responsiveness of the private partner, the fact that the private partner maintains regulatory compliance, and the fact that the private partner works in a seamless manner with the municipality.

Municipal officials also point out some areas that need to be improved. These include reducing backlogs for preventive maintenance as well as lowering prices, but neither was mentioned by more than one respondent.

Most of those interviewed were not newcomers to partnerships. Seventy percent of the municipalities surveyed had experience under a prior outsourcing contract.

Further, most of the municipalities plan to continue with a partnership when the current contract expires. Respondents rated their likelihood to outsource again on a scale of one to five—with five being “likely,” three being “possibly,” and one being “definitely will not.” The average response was a 4.6, with 76 percent of respondents giving a 5; 14 percent, a 4; 7 percent, a 3; and 3 percent, a 1.

Only one municipality will definitely not outsource again. This municipality purchased the plant from its current partner, which had formerly run the plant as a privatized operation. Part of the sales agreement entailed creating a partnership with the previous owner in order to educate the municipality on the operation of the plant. Before the contract was entered into, city officials indicated they would not continue with a partnership arrangement after the term of this special arrangement. Besides this anomaly, most municipalities surveyed will likely outsource again.

*“A city like ours is just too small to garner the expertise that they [the private partner] have in this area because they operate other plants in the area. Small towns cannot hire that expertise—especially with the ever-changing rules and regulations.”*

— JAMES CROSBY, CITY MANAGER  
YUKON, OKLAHOMA

*“The most beneficial attribute is that we get professional management from the operators [private partner].”*

— CARLTON CURRY, DIRECTOR OF  
CONTRACTS AND OPERATIONS  
INDIANAPOLIS, INDIANA

*“As a city, we dabble in everything. They are specialized. They have the expertise that far exceeds what we could provide our customers.”*

— DEAN MAZZARELLA, MAYOR  
LEOMINSTER, MASSACHUSETTS

*“The singular focus on making the plant run is the most beneficial attribute of the partnership. There is also a joint vision that we all share. Really, working together as one staff to achieve both of our goals.”*

— PAUL SHOENBERGER, CHIEF OF  
ENGINEERING & OPERATIONS,  
WEST BASIN MUNICIPAL WATER  
DISTRICT, EL SEGUNDO, CALIFORNIA

*“They are very responsive, and when there are problems, I usually do not have to follow up on it very closely. They take care of it.”*

— RAY SHELL, P.E., UTILITY MANAGER  
GLYNN COUNTY, GEORGIA

*“We originally brought in a partner because the city lost its operators to other jobs, and the city realized that wastewater treatment plant operators fluctuate a lot, and it is difficult to get them. A partner could manage the staffing.”*

— JOSE GIL, CITY ENGINEER/PUBLIC  
WORKS DIRECTOR  
DADE CITY, FLORIDA



## SMS EXHIBIT 1

*"We were originally forced by court order to outsource. Our original premise was to take [responsibility for operations and maintenance] back after the contract ended, but we did not know where we would get expert operators from. And, we were happy with things the way they were going."*

— VINNY FURTADO, SUPERINTENDENT  
OF WASTEWATER DIVISION  
NEW BEDFORD, MASSACHUSETTS

*"This is the first time I have been involved with a utility contractor in my 30 years with state government. I have always spurned it in my past positions because I did not see any major benefit, and I perceived a loss of control, but this is a great relationship."*

— STEVE ROUTH, PUBLIC WORKS DIRECTOR  
REIDSVILLE, NORTH CAROLINA

*"I cannot say enough about the quality of service we have been given. I have been with the municipality for 25 years. I think it is one of the best operational decisions that the municipality has made in the past 15 years."*

— PATRICIA SPADE, BOROUGH MANAGER  
BOYERTOWN, PENNSYLVANIA

*"One benefit is the level of expertise we get from the top down—from their central office. It is like having a number of consultants permanently on staff."*

— NAN CROSSLAND, EXECUTIVE DIRECTOR  
DEDHAM-WESTWOOD, MASSACHUSETTS

*"The [private partner] has, at its disposal, engineering firms and an expertise at a higher level that can be drawn in as needed. There are resources there that we would not normally have."*

— DARRELL FONESCA, CITY MANAGER  
DOS PALOS, CALIFORNIA

Survey respondents expressed their own views on the potential for continued outsourcing but noted that the final decision was usually up to the city council. However, in most cases, the city council accepts the recommendation of those who supervise the partnership and would be left to run the previously outsourced facilities if the municipality took back operations. These are the people that responded to the survey.

Not only are municipalities satisfied with the partnerships in general, but they also are satisfied with their current partners. In 86 percent of the cases where the current partnership was preceded by an outsourcing arrangement, the public partner awarded the contract to the incumbent private partner either through negotiation or through competitive bid. *Exhibit 1* shows how current partners were chosen when a partnership previously existed.

### Exhibit 1

Current partnerships that were previously outsourced

Competed for and won by the incumbent	24%
Competed for and won by a new bidder	14%
Negotiated with the incumbent	62%

General satisfaction is often related to satisfaction with the technical competence of the private partner and the quality of communication between the private and public partner. Technical competence is essential to running the plant efficiently. Communication with the city is imperative to ensuring an effective working relationship between the public and private partner.

Respondents rated technical competence on a scale of one to five—with five being "outstanding," three being "satisfactory," and one being "poor." The average rating was 4.4, with 50 percent of respondents rating their private partner a 5; 43 percent, a 4; and 3 percent, a 2. Specific reasons mentioned by respondents for their high ratings include:

- The private partner found the wastewater treatment odor problems and fixed them
- The private partner is able to bring in outside expertise and focus on training for the employees
- The private partner keeps the municipality in compliance

Many respondents report the benefit of leveraging the expertise of employees throughout the company. One respondent even congratulated its private partner on keeping the plant running efficiently and in compliance while the plant was under construction and being expanded.

Respondents also point out several areas where their private partners could improve their technical competence in order to get an even higher rating. One municipality points out that staffing needs to be improved during peak storm periods, specifically during hurricanes. Another believes that there is too much operator turnover at the facility.

## SMS EXHIBIT 1

One municipality rates its private partner's expertise as less than satisfactory. This respondent did so because the private partner did not have a project team in place when the contract was initiated. The private partner had to locate and hire operators. In doing so, they were unable to hire the best qualified operators. However, the respondent believes that the operators are now up to speed and are very competent.

Communication between the private partner and the municipality also is highly rated by respondents. Respondents rated the quality of communication on a scale of one to five—with five being “outstanding,” three being “satisfactory,” and one being “poor.” On average, respondents rate the quality of communication as 4.5, with 57 percent of respondents rating their private partner a 5; 33 percent, a 4; and 10 percent, a 3. Respondents rate communication high because they and their private partners hold regular meetings, and the private partners inform the municipality of any potential issues before they become problems. Some respondents mention areas for improvement. One respondent would like to hear information sooner than they currently do, and another would like the private partner to better communicate its role to the residents of the municipality.

*Public Works Financing*'s data confirms the survey results that municipalities are very satisfied with both the partnerships and their partners. *Public Works Financing*'s latest annual outsourcing survey<sup>3</sup>, with additional data collected by Water Partnership Council staff, shows that more than 92 percent of the 560 government contracts up for renewal in 2004 were again outsourced either to the incumbent or to another market participant. Almost 91 percent of contracts up for renewal were won by the incumbent, and slightly more than 2 percent were won by another market participant. Less than 6 percent of systems up for renewal reverted back to the municipality, and less than 2 percent were not renewed for other reasons.

### IMPACT ON THE ENVIRONMENT

One benefit of partnerships cited by respondents is the positive impact on the environment. In fact, many respondents cite improving environmental stewardship as the main reason they enter into a partnership. This survey uses regulatory compliance to measure environmental stewardship.

Municipalities work with their private partners to bring the municipality back into regulatory compliance efficiently and cost-effectively. In fact, 74 percent of the respondents mention that regulatory compliance is better under the partnerships than before the partnerships (see *Exhibit 2*). In many cases, the private partners perform better than the regulations require. In some cases municipalities received awards for their outstanding level of regulatory compliance.

*Exhibit 2* shows that regulatory compliance deteriorated in one municipality. In this case the municipal official indicated that ongoing expansion of the plant made consistent compliance difficult.

#### Exhibit 2

Current regulatory compliance  
as compared to before the partnership

Better	74%
Equal	22%
Worse	4%

<sup>3</sup> *Public Works Financing*, March 2005, Volume 192.

*“Communication is open, free flowing, and honest. At any time I can call their project general manager or the janitor if I feel he can answer the question I have.”*

— JOHN JANKOWSKI, CONTRACT  
COMPLIANCE OFFICER  
MILWAUKEE, WISCONSIN

*“Much of the push was because of some compliance issues with the wastewater treatment plant that the city could not resolve. We hired them for the expertise that they have to run our plant and to keep us in compliance with regulations that are getting more difficult every day.”*

— STEVE EDDY, CITY MANAGER  
MOORE, OKLAHOMA

*“What they do well is exceed their permit requirements. They come in under what the permit allows.”*

— DAN COODY, MAYOR  
FAYETTEVILLE, ARKANSAS

*“Before we brought our partner in, we had 10 years of non-compliance. We have not been out of compliance since. We have received awards for our compliance from Save the Bay.”*

— SUSAN MENARD, MAYOR  
WOONSOCKET, RHODE ISLAND

*“We received an award for our environmental compliance.”*

— VANESSA ROW, FINANCE OFFICER  
KEYSTONE, SOUTH DAKOTA

*“We are in much better compliance now than we ever were as a public entity.”*

— JAMES BURNETT, MAYOR  
FREEPORT, TEXAS

*"I see a lot more communication between our partner and the regulatory agencies. Our partner communicates the importance of having communication with the regulators to its operators."*

— JOSE GIL, CITY ENGINEER/PUBLIC WORKS DIRECTOR  
DADE CITY, FLORIDA

*"Compliance is a huge issue—trying to comply with regulations that change by the minute is impossible for the city to do. It is unfair to the public to try to masquerade that the city itself can keep up on all these things."*

— DEAN MAZZARELLA, MAYOR  
LEOMINSTER, MASSACHUSETTS

*"Odor complaints went down tremendously."*

— SUSAN MENARD, MAYOR  
WOONSOCKET, RHODE ISLAND

Private partners are able to excel in the area of regulatory compliance because they have the technical expertise and because they develop strong relationships with regulators. Private partners know what the regulations are, when they will change, and what to do if there is a problem.

Many respondents mention that environmental regulations seem to change on a daily basis, and that they find it overwhelming to try to keep up with these changes. On the other hand, they see private partners as being in the business of tracking regulations, with trained personnel to do so. Private partners are proactive versus reactive in how they track and manage regulations.

In addition, the private partner has a large incentive to be in compliance—if a plant

is out of compliance, the private partner is often responsible for the fines. Respondents believe that this focus on environmental compliance is coming straight down from the highest levels of their private partner companies—that it is something ingrained in the cultures of these companies.

## IMPACT ON CUSTOMERS

Partnerships are meant to be seamless to the customer. Nevertheless, partnerships often benefit the customer, or at the least, have no negative impact on the customer.

This report uses three criteria to evaluate the impact on customers. The first is the frequency of customer complaints in comparison to before the partnership was initiated. The second is how customer rates have changed during the partnership. The third is whether the private partner makes a positive contribution to the community—and ultimately the customer—above and beyond what is mandated in the contract.

In 37 percent of the partnerships surveyed, customer complaints decreased (see *Exhibit 3*). Most of these are related to reducing wastewater treatment odors. In most cases, the number of customer complaints remained the same. In two cases, the frequency of customer complaints increased after the partnership began. One of these cases is the result of the wastewater plant undergoing expansion. Often, construction work negatively impacts operations, which leads to increased odors for a short amount of time. In general, however, customer complaints remained the same or decreased.

One respondent lauds his private partner for locating the areas that were causing odor problems and fixing them. Another respondent has so much faith in his private partner that the municipality wants to expand the scope of the contract to cover other odor-causing areas that are run by the municipality. This respondent believes that his private partner will be able to help the municipality reduce the odor problems and, therefore, the number of complaints.

### Exhibit 3

Current frequency of customer complaints as compared to before the partnership

More	7%
Equal	56%
Less	37%

## SMS EXHIBIT 1

A second consumer impact is customer rates. Water and sewer rate changes are not determined by the private partner; the municipality sets the rates. In some cases, the municipality can keep rates down due to the cost savings that the partner achieves. However, for the most part, respondents thought their partnerships had no impact on rates. Seventy-five percent of the municipalities surveyed had some change in rates during the partnership. Seventy-six percent of those respondents thought the rate change would have been the same under city operation (see *Exhibit 4*).

### Exhibit 4

How rate change compares to pre-partnership projections

More	6%
Equal	76%
Less	18%

Three respondents believe that their partnerships resulted in smaller rate increases than would otherwise have been implemented. One of these municipalities bases this on the city's ability to run with a leaner staff under its private partner, saving the ratepayers money.

One municipality notes that its rates increased under the partnership more than they otherwise would have. This respondent believes that the municipality could run the operations more efficiently. However, this same respondent attributes the municipality's strong record of regulatory compliance to its private partner.

A third consumer impact involves private partner activities beyond the operation and maintenance of the facilities. In many communities, private partners make a contribution to the community beyond what is required in their contracts. Ninety-three percent of respondents note that their private partners actively participate in community activities. Areas where the private partner gets involved include the following:

- Giving tours
- Developing curricula for local schools
- Hosting stream cleanups
- Donating to charitable causes and events
- Providing bottled water for events
- Sponsoring employee and community picnics

Two municipalities believe that their partners do not go above and beyond their contracts in giving back to the community. One of these does not want its private partner to do so because the municipality believes that the cost of doing so will be passed back to the municipality. In this case, however, the contract does mandate a college scholarship to be provided by the private partner. The other municipality is pleased with the services provided by its private partner and is not disappointed that the private partner has not been more involved with the community.

*"With a private contractor managing the facilities for us, we do not need as many oversight positions at Borough Hall. That has been a cost savings to the citizens and users."*

— PATRICIA SPADE,  
BOROUGH MANAGER  
BOYERTOWN, PENNSYLVANIA

*"Cost savings were achieved and exceeded. We reduced the rates [user fees] by 15.6 percent in the first year because our partner reduced our costs so greatly."*

— JOHN JANKOWSKI, CONTRACT  
COMPLIANCE OFFICER  
MILWAUKEE, WISCONSIN

*"By entering into a partnership, we were able to freeze rates for five years. We avoided a 32 percent rate increase."*

— CARLTON CURRY, DIRECTOR OF  
CONTRACTS AND OPERATIONS  
INDIANAPOLIS, INDIANA

*"They participate in other groups in town just like they are employees of the town even though they are an independent contractor."*

— JOHN MINTA,  
COUNCIL PRESIDENT  
CLARKSVILLE, INDIANA

*"They have a very nice program working with local schools. They also have a couple of nice programs where they get the public at large involved in cleanups such as 'beach sweeps.'"*

— JOHN JANKOWSKI, CONTRACT  
COMPLIANCE OFFICER  
MILWAUKEE, WISCONSIN

## IMPACT ON MUNICIPALITIES

The overview of this report identified a variety of reasons why municipalities enter into partnerships. One of these reasons is cost savings—many municipalities believe that a private partner can be more efficient in running a plant. However, this study has shown that, although many municipalities achieve cost savings, this may not be the primary driver.

Only 46 percent of the surveyed municipalities projected cost savings before entering the partnership. Ninety-two percent of those respondents note that projected cost savings were achieved, and the other 8 percent note that they are too early in the contract term to know whether the costs savings will be achieved. Savings ranged from 5 percent to 25 percent. Respondents mention that their private partners were able to keep costs down by:

- Leveraging their size and making high-volume purchases for supplies such as chemicals
- Running the plants with fewer personnel
- Investing in technology
- Reducing overhead costs
- Performing preventive maintenance

What about the other 54 percent of municipalities that did not project cost savings when they entered into partnerships? Although those municipalities may be receiving cost savings, they also may have entered into the partnership because they were out of environmental compliance or because the municipality did not have the appropriate personnel.

All of those municipalities that did not project costs savings report that regulatory compliance was equal (17 percent) or better (83 percent) and that their partners make a positive contribution to the community above what is required in the contract (100 percent). One of the respondents that did not project cost savings entered into the partnership because the municipality had an accident that cost lives. At that time, the municipality realized that it could not safely run all of its operations.

In summary, the survey results show that municipalities enter into partnerships for more than just financial considerations.

*“I do not think we would be seeing the kinds of savings they [the private partner] are realizing for us without them because of the volume of their purchases.”*

— PATRICIA SPADE,  
BOROUGH MANAGER  
BOYERTOWN, PENNSYLVANIA

## IMPACT ON EMPLOYEES

Private operation typically results in better educational and training opportunities for employees. For both the private partner and the public facility owner, enhanced training translates to better-run, more efficient, and environmentally sound facilities. For the employees, enhanced training means more opportunities for professional growth and advancement.

Respondents mention that, in general, employees are very satisfied with their partnerships. Initially, employees are apprehensive about being an employee of a private firm as opposed to working as a municipal employee. They fear job loss, reduced salaries and benefits, and loss of union representation. In 29 percent of the partnerships surveyed, the municipality required contractually that the private partner increase or maintain salary and benefit levels.



## SMS EXHIBIT 1

In many cases, the employees have the option of staying with the city, taking a buyout, or being hired by the private partner. Respondents indicate that the vast majority who had these options chose to go to the private partner. They also note that morale and satisfaction increase as employees get comfortable with the partnership and their new employers. One even notes that an opportunity arose for the employees to return to city employment well into the partnership, and the employees chose not to do so.

Respondents rate average employee satisfaction as a 4 on a scale of one to five—with five being “extremely satisfied,” three being “satisfied,” and one being “not satisfied at all.” The average response was a 4, with 21 percent of respondents rating employee satisfaction a 5; 58 percent, a 4; and 21 percent, a 3. No one rates employees as not being satisfied at all.

Some municipal employees are represented by unions. Thirty-eight percent of the municipalities surveyed had union representation prior to the partnership. Twenty-one percent currently have union representation under the partnership.

Employee grievances are another measure of employee satisfaction. None of the respondents who still have contact with employees report an increase in employee grievances under the partnership (see *Exhibit 5*). In fact, most report a decrease.

### Exhibit 5

Current number of employee grievances  
as compared to before the partnership

More	0%
Equal	36%
Fewer	64%

Of those that were previously unionized and are no longer, 50 percent say there are fewer grievances, and the other 50 percent report that the number of grievances remained the same.

In many cases, at the start of the partnership, employees were concerned that they would lose their jobs due to a private partner’s efforts to make money by reducing staff costs. Involuntary employee turnover is a measure of whether private partners “clean house” once the partnership begins. In 33 percent of the cases, involuntary employee turnover declined under the partnership (see *Exhibit 6*). In the one case where involuntary employee turnover increased, the respondent notes that the private partner needed to bring in more qualified staff. The number of positions did not change, just the people who were in those positions.

### Exhibit 6

Current involuntary employee turnover  
as compared to before the partnership

More	7%
Equal	60%
Less	33%

*“We [the city] have gone through some tough times since then [the beginning of the partnership], so we probably would have ended up laying off somebody, and they ended up being able to keep their jobs.”*

— DARRELL FONSECA,  
CITY MANAGER  
DOS PALOS, CALIFORNIA

*“It is such a large organization that the employees can move and go wherever the opportunities present themselves.”*

— JOHN MINTA,  
COUNCIL PRESIDENT  
CLARKSVILLE, INDIANA

*“A private company does a much better job of training its staff than a municipality does in general terms. I know they are doing a much better job than we were doing.”*

— PATRICIA SPADE,  
BOROUGH MANAGER  
BOYERTOWN, PENNSYLVANIA

*“We were a little concerned about that [employee salaries decreasing], but actually the salaries went up a little bit, and they got some additional benefits.”*

— JAMES BURNETT, MAYOR  
FREEPORT, TEXAS

## SMS EXHIBIT 1

### Exhibit 7

Current education and training opportunities as compared to before the partnership

More	93%
Equal	7%
Fewer	0%

### Exhibit 8

Current professional development and advancement opportunities as compared to before the partnership

More	93%
Equal	7%
Fewer	0%

### Exhibit 9

Current financial compensation as compared to before the partnership

More	53%
Equal	34%
Less	13%

### Exhibit 10

Current employee benefits as compared to before the partnership

More	20%
Equal	40%
Fewer	40%

Multiple respondents note that the private partners were able to achieve efficient staffing levels by not replacing individuals who left voluntarily.

Employees are always looking for ways to increase their skills and education and to move into positions that offer more responsibility or higher salaries. Ninety-three percent of respondents state that employees have more educational and training opportunities with their private partners than they did with the municipality (see *Exhibit 7*). Furthermore, 93 percent indicate employees have more professional growth and advancement opportunities as employees of the private partner (see *Exhibit 8*).

Respondents note that their private partners are better at instituting structured training plans and programs. In addition, respondents state that the private partners are able to offer job opportunities in other plants throughout the country. This allows operators to advance when opportunities are not available in a given municipality.

Financial compensation and benefits are crucial to employee satisfaction. Respondents note that in 53 percent of the cases, employees receive higher salaries under the partnership (see *Exhibit 9*). Respondents believe that this is a result of a private partner's ability to offer bonuses or profit-sharing.

In two cases, the employees receive lower salaries under the partnership. In one of these cases, employees are leaving the partner to make more money at other plants with other private partners or municipalities. The respondent notes that this may be a result of the employees becoming more marketable due to the reputation of the private partner and the training the private partner provides. In the other case, employees are trying to return to the municipality, which pays very competitive salaries in relation to other employers in the area.

Of the municipalities that did not contractually require maintaining or increasing financial compensation, respondents note that in 33 percent of the cases financial compensation increased, in 11 percent of the cases it decreased, and in 56 percent of the cases it remained the same.

Benefits under partnerships do not fare as well as financial compensation, training, and advancement opportunities. Respondents report an increase in benefits in only 20 percent of the cases (see *Exhibit 10*). In 40 percent of the cases, benefits decreased. In most cases where there was a decrease, financial compensation was greater under the partnership. In two cases, however, financial compensation and employee benefits were both worse under the partnership.

Of the municipalities that did not contractually require maintaining or increasing employee benefits, respondents note that in 23 percent of the cases benefits increased, in 33 percent of the cases they decreased, and in 44 percent of the cases they remained the same.

With the exception of benefits, employees of partnerships tend to benefit from better training, advancement opportunities, and financial compensation.

## APPENDIX A — Survey Instrument

The following is the telephone survey questionnaire.

1. What types of operations does the contract cover?
  - a. Water treatment
  - b. Wastewater treatment
  - c. Water and wastewater treatment
  - d. Other:
2. What is the size of the facility(ies) in mgd? \_\_\_\_\_ mgd
3. What is the length of the collection/distribution system in miles of sewer or water lines?  
\_\_\_\_\_ miles
4. What population is served by this facility(ies)? \_\_\_\_\_ people
5. What is the duration of the contract? \_\_\_\_\_ years
6. When did private operations commence under the current contract?
7. Were the operations of this facility (or facilities) outsourced prior to this contract?
  - a. Yes
  - b. No
8. If yes, was it
  - a. Re competed and won by the incumbent private partner
  - b. Re competed and won by a new bidder
  - c. Renewed without competition to the incumbent private partner
9. What are your general comments on employee satisfaction and opportunities before and after the partnership?  
Comments: \_\_\_\_\_
10. Was there union representation while the facility was under public management?
  - a. Yes
  - b. No
11. Is there currently union representation?
  - a. Yes
  - b. No
12. What is the current frequency of employee grievances?
  - a. More than before the partnership
  - b. Equal to before the partnership
  - c. Less than before the partnership  
Comments: \_\_\_\_\_



## SMS EXHIBIT 1

13. How does involuntary employee turnover compare to before the partnership?

- a. More than before the partnership
- b. Equal to before the partnership
- c. Less than before the partnership

Comments: \_\_\_\_\_

14. How do educational and training opportunities compare to before the partnership?

- a. More than before the partnership
- b. Equal to before the partnership
- c. Less than before the partnership

Comments: \_\_\_\_\_

15. How do professional growth and advancement opportunities compare to before the partnership?

- a. More than before the partnership
- b. Equal to before the partnership
- c. Less than before the partnership

Comments: \_\_\_\_\_

16. How does employee financial compensation compare to before the partnership?

- a. More than before the partnership
- b. Equal to before the partnership
- c. Less than before the partnership

Comments: \_\_\_\_\_

17. How do employee benefits compare to before the partnership?

- a. More than before the partnership
- b. Equal to before the partnership
- c. Less than before the partnership

Comments: \_\_\_\_\_

18. Was an increase in benefits and/or financial compensation criterion used for evaluating competitive proposals during the procurement process?

- a. Yes
- b. No

19. How would you judge overall employee satisfaction with the private partnership on a scale of 1 to 5 with 5 being extremely satisfied, 3 being satisfied, and 1 being not satisfied at all?

1 2 3 4 5

Comments: \_\_\_\_\_

## SMS EXHIBIT 1

20. How does regulatory compliance compare to before the partnership?

- a. Better than before the partnership
- b. Equal to before the partnership
- c. Worse than before the partnership

Comments: \_\_\_\_\_

21. What is the frequency of customer complaints compared to before the partnership?

- a. More than before the partnership
- b. Equal to before the partnership
- c. Less than before the partnership

Comments: \_\_\_\_\_

22. Has your partner made a positive contribution to the overall community?

- a. Yes (If yes, in what ways?)
- b. No

Comments: \_\_\_\_\_

23. How do you ensure that the private partner of your facility is acting in the public interest?

Comments: \_\_\_\_\_

24. Do/did the terms of the contract project cost savings?

- a. Yes
- b. No

25. If yes, were cost savings achieved?

- a. Yes
- b. No

26. If yes, what is the projected/realized cost savings resulting from the partnership?

- a. In dollar value? \$ \_\_\_\_\_
- b. In percentage terms? \_\_\_\_\_ %

27. If yes, in what area(s) has your private partner reduced costs?

Comments: \_\_\_\_\_

28. Have customer rates changed under the partnership?

- a. Yes
- b. No

## SMS EXHIBIT 1

29. If yes, how does this change in rates compare to what was projected prior to the partnership?

- a. More than was projected before the partnership
- b. Equal to what was projected before the partnership
- c. Less than what was projected before the partnership

Comments: \_\_\_\_\_

For this section of questions, please answer on a scale of 1 to 5 with 5 being outstanding, 3 being satisfactory, and 1 being poor.

30. Technical performance and capabilities of your private partner 1 2 3 4 5

Comments: \_\_\_\_\_

31. Communications between your partner and the city 1 2 3 4 5

Comments: \_\_\_\_\_

32. What is the overall satisfaction of the public agency with the partnership, with 5 being extremely satisfied, 3 being satisfied, and 1 being not satisfied at all? Please feel free to provide additional comments.

1 2 3 4 5

Comments: \_\_\_\_\_

33. What is the potential that the services currently provided by the private partner will continue to be outsourced, with 5 being likely, 3 being possibly, and 1 being definitely not?

1 2 3 4 5

Comments: \_\_\_\_\_

34. What do you consider the most beneficial attribute(s) of the partnership?

Comments: \_\_\_\_\_

35. Do you have any final comments you would like to share about your partner or partnership?

Comments: \_\_\_\_\_

May I consider this interview to be on the record?

On Off

Would you be willing to allow me to quote you?

Yes No



## SMS EXHIBIT 1



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## SMS EXHIBIT 2

*The Committee on Energy and Commerce***Joe Barton, Chairman**  
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# Witness Testimony

**Mr. Donald L. Correll**

President and CEO  
Pennichuck Corporation National Association of Water Companies  
1725 K Street NW, Suite 1212  
Washington, DC, 20006

[Tapped Out? Lead in the District of Columbia and the Providing of Safe Drinking Water](#)  
Subcommittee on Environment and Hazardous Materials  
July 22, 2004  
09:30 AM

Mr. Chairman and members of the subcommittee, thank you for the invitation to testify before you today.

My name is Donald Correll. Since August of 2003 I have served as President and CEO of Pennichuck Corporation. Pennichuck Water Works was founded in 1852 and has grown to become the largest investor-owned water company in the state of New Hampshire, serving a population of 120,000 people in 22 communities throughout southern New Hampshire and in Massachusetts.

Pennichuck Corporation is a holding company with five wholly owned operating subsidiaries. The Company is comprised of three private water utilities, Pennichuck Water Works, Inc., Pittsfield Aqueduct Company and Pennichuck East Utility that are regulated by the New Hampshire Public Utilities Commission, and two non-regulated companies, Pennichuck Water Service Company and The Southwood Corporation. Pennichuck is the oldest continuously operated company in New Hampshire.

Prior to joining Pennichuck, from 1990 to 2001, I served as Chairman and CEO of United Water, one of the largest water service companies in the United States with operations and investment in 19 states, Canada, Mexico and the UK. I also serve as an advisory director with Underground Solutions Inc., a

## SMS EXHIBIT 2

water technology and service company, based in Sarver, Pennsylvania, which is involved in the water infrastructure industry.

I am testifying today on behalf of The National Association of Water Companies, NAWC is the only national organization exclusively representing all aspects of the private and investor-owned water industry. The range of our members' business includes ownership of regulated drinking water and wastewater utilities and the many forms of public-private partnerships and management contract arrangements. NAWC has more than 150 members, which in turn own or operate thousands of utilities in 38 States around the country.

**ROLE OF THE PRIVATE SECTOR**

The private sector has long played a vital role in the provision of water in our nation, and stands ready to do much more. The privately owned water utility business traces its roots back to before the very existence of our nation. And today, one out of every six Americans receive their drinking water service from a private water company.

However, outright private ownership is but one-model localities can pursue as a means of addressing their infrastructure challenges. Another large and growing option is some form of public-private partnerships, including contract operations, wherein the municipality retains ownership of the asset; in this case a water utility and its infrastructure, but the management and operations of the facility are contracted out to a private company.

Management contract or public-private partnership arrangements between municipalities and private companies represent a newer model (started in the 1970s), and have become hugely popular in a very short period of time. Today, private firms operate more than 2,400 publicly owned water and wastewater facilities for nearly 2,000 municipalities. Such arrangements have proven to be very popular with municipalities and enjoy a 90% contract renewal rate.

History has shown that the private sector can and does provide the public with safe and efficient water service through market-based solutions. The private water industry has been on the cutting edge of technical innovation and research. Furthermore, in this time of increased utility security awareness, the private sector has once again been on the forefront of these initiatives, bringing to the industry firsthand security experience derived from working in some of the world's hot spots.

## SMS EXHIBIT 2

**THE AGING INFRASTRUCTURE CHALLENGE AND SOLUTIONS**

NAWC commends the Subcommittee for tackling the complex issue of safe drinking water and specifically the lead problems we have seen. Many of the issues are related to the broader infrastructure problem this committee has been looking at for some time. Let me start there, and then I will talk specifically about the lead issue.

It has been well established from a number of sources that cities, towns and utilities face a major challenge over the next several decades replacing aging and worn-out drinking water infrastructure. According to the EPA infrastructure gap analysis, issued in 2002, drinking water systems will spend between \$154 and \$446 billion through 2019. Wastewater systems will spend between \$331 and \$450 billion over that same period. In addition to EPA, the Congressional Budget Office and the General Accounting office have done studies on the country's infrastructure challenge and their cost estimates are similar to EPA's.

Utilities and localities must take the lead in addressing this infrastructure challenge by accessing the many organizational, managerial and financial tools at their disposal. Clearly, the Federal Government has a role in assisting with this challenge, but that role does not need to be taking on the major financial responsibility for infrastructure. Instead the role should be to encourage utilities to pursue smart business-like management practices including improving operating efficiencies to free up cash for infrastructure replacement, charging what it costs to provide the service including capital investments, selecting cost-effective infrastructure replacement technologies, and implementing an infrastructure replacement program that will assure the utility's viability.

Public-private partnerships can often provide a proven model for accomplishing all of the above.

Direct government loan assistance to utilities is another government role, but, like the Drinking Water-SRF, should be carefully managed and targeted only where and when necessary. An inappropriate role of government would be to subsidize the water industry indefinitely with a massive federal grant program, as some have advocated.

Grants are a very inefficient method of providing assistance to utilities. Grants send the wrong conservation signals and can result in bad management practices,

The Construction Grants Program of the 1970s had many problems, which could very likely be reborn if a



## SMS EXHIBIT 2

similar program were reconstituted. Those problems included procurement regulations that discounted quality for the sake of lowest price, lack of reliable capital replacement accounts to ensure that funds exist for future replacement (such as today), and little local buy-in or ownership on the part of grant recipients, which resulted in sometimes wildly overbuilt systems and wasted tax dollars.

The best means for providing federal funds are the State Revolving Loan Funds along with the use of creative and innovative solutions. We can make considerable progress toward solving our infrastructure needs by avoiding the mistakes of the past and securing our water infrastructure for the future. I encourage Congress therefore to retain the State Revolving Loan Funds as the primary conduit of assistance to water utilities.

Congress should also ensure that Federal assistance is used to encourage strong management practices by water utilities. This should include full cost of service rates, asset management, consolidation and support for public-private partnerships.

**Full Cost of Service Rates**

Across the country, many water utilities are charging customers water rates that are misleading and do not cover the cost of providing the service. This has resulted in a devaluation of water as resource, which not only causes utilities to rely on federal subsidies for investment in infrastructure replacement, but also sends the wrong signals to consumers about the value of water and the need for conservation.

In some cases the actual cost of providing water service is greater than the rates charged by utilities. In fact, Dr. Janice Beecher of Beecher Policy Research said before this Subcommittee in March of 2001

"...when municipalities provide electricity and natural gas services, revenues exceed total capital and operating expenditures. For water and sewer services... total expenditures exceed revenues. The findings generally suggest that municipal water customers do not cover expenditures through rates and other user charges."

Also, in a study on this issue released by the General Accounting Office, they found the amount of funds obtained from user charges and other local sources of revenue was less than the full cost of providing service for over a quarter of drinking water utilities. Indeed many municipalities pride themselves on their low rates, and publish their comparative rates as being lower than other when in fact, they are not charging the full cost of service.

## SMS EXHIBIT 2

This clearly demonstrates the need for full cost of service rates. Utilities must be able to generate the revenue needed to cover costs and invest in replacing aging infrastructure. This can only happen when we are charging customers the true cost of the services provided.

However, NAWC recognizes that increasing rates will put low-income families at risk of not being able to afford their water bills. To address this, NAWC supports a federal water rate payer assistance program modeled after the Low-Income Home Energy Assistance Program (LIHEAP).

However, we do not believe that the increased rates will be an overwhelming burden for most Americans. According to the Congressional Budget Office, Americans currently pay roughly 0.5% of their total household income for water and wastewater service. This is significantly less than other utility costs, which range from 2% to 5% of household income, and suggest room for increases.

### **Asset Management**

Generally, privately owned and operated utilities manage their infrastructure assets, such as pipelines and other equipment to maximize the useful lives of the assets, increase efficiency, minimize costs, and maintain service to customers. Careful management of assets is essential if we are to successfully meet the infrastructure financing challenge. However, many localities do not have in place such asset management plans. In fact the General Accounting Office has estimated that as many as 25% of all utilities do not have such a plan.

Since good management of assets can go along way toward avoiding an infrastructure-financing gap as well as addressing the infrastructure replacement challenge, NAWC believes utilities should adopt such practices. Congress should therefore encourage, as part of the SRF Funding process, the implementation of sound asset management practices.

### **Consolidation**

There are over 50,000 community water systems in the United States today, many of which are very small. In many, but not all cases, the financial challenges facing these utilities can be addressed by improving their economies of scale through consolidation. By tying consideration of SRF funding to consolidation, Congress will encourage utilities to put aside parochial interests, expand their vision and improve the service to customers. Over the last five years, Pennichuck has consummated dozens of acquisitions of smaller systems, many of which would

## SMS EXHIBIT 2

not have financially viable over the long-term. It is important to note, that consolidation does not work everywhere, and is not the answer for all problems. However, it is clear that consolidating ownership and/or management functions with other facilities can streamline a utility and save money.

### **Public-Private Partnerships**

Municipalities large and small all over the country have realized great savings and success through partnerships with private firms. These partnerships take many forms, from contracting out small portions of a utility's operations such as billing or meter reading, to multi-year all inclusive management contracts wherein a private firm runs and manages all aspects of a municipally owned utility, to the transfer of assets to a private company. Cost savings that localities have realized over the years from such arrangements range up to 40%, freeing up much needed capital for infrastructure replacement, without burdening either the customer or the American taxpayer. Likewise these arrangements have often allowed municipalities to avoid significant rate adjustments while still meeting the higher EPA water quality standards.

Therefore Congress should, whenever appropriate, encourage the development of such partnerships as a tool for addressing our infrastructure replacement challenges.

### **Access to State Revolving Loan Funds for Private Water Companies**

Access to the DW-SRF (and the Clean Water SRF for that matter) should be based on need and need alone. The ownership of the utility should not be a factor. After all, it's the taxpayers, all taxpayers, not just those of municipal utilities that fund The SRFs.

When Congress established the DW-SRF in 1996 they knew that the benefits of the SRF would flow to the customers of privately owned utilities, not the owners or stockholders. And this is working well in many states. NAWC has many examples of privately owned utilities working with States, receiving SRF assistance and extending service to underserved or badly served populations. These are some of the best examples of public-private partnerships.

However, we regret to report that there are still ten States (Alabama Arkansas, Colorado, Georgia, Kansas, Mississippi, North Carolina, Oklahoma, Tennessee, Wyoming) that, despite Congress's clear intent, do not allow private utilities access to the DW-SRF. Incredibly, these States are still allowed to use private utilities in their needs survey, and thus receive

## SMS EXHIBIT 2

SRF capitalization grant funds based on this private utility need, a need they have no intention of meeting. NAWC believes that Congress should only allow EPA to provide SRF allocation grants to the States for the needs the State is willing to actually meet. If a State does not allow private utility access to the DW-SRF, EPA should reduce their allocation grant accordingly.

Also, I must report that in some of the states that allow private access to the SRF, there are often burdensome application requirements and fees that, in some cases, municipal utilities don't face. Also in some States, their priority lists clearly favor municipally owned utilities, and the needy private utilities often receive little or no funding.

These processes are not in line with Congressional intent when you granted private utility access to the SRF. We hope to continue working with you on these issues.

### **Private Activity Bonds**

Another role that the federal government, and specifically Congress can play is passing legislation to eliminate the state volume caps on Private Activity Bonds (PABs) for water and wastewater projects, thus providing billions of dollars in capital that can be used to invest in water infrastructure replacement. Changing the tax code and exempting water and sewage facilities from the state volume caps could be one of the most productive incentives Congress can provide to stimulate infrastructure investment and replacement. In fact, billions of potential investment will be stimulated by the tax change but it will cost the federal government less than \$150 million over ten years, according to the Joint Committee on Taxation.

I understand that this issue does not fall under the jurisdiction of this Committee, however it is an important tool for addressing the infrastructure challenge, and therefore, I wanted to bring it to your attention.

### **LEAD AND DRINKING WATER**

Lead is a naturally occurring metal that was used regularly in a number of industrial capacities for most of the 20th Century. Lead was used as a component of paint, piping (including water service lines), solder, brass, and as a gasoline additive until the 1980's. According to the U.S. Environmental Protection Agency (USEPA), lead paint and the contaminated dust and soil it generates is the leading household source of lead exposure today. Research has confirmed that lead is highly toxic. Ingestion of lead can pose a serious health risk to humans, especially

## SMS EXHIBIT 2

children.

Lead contamination in drinking water almost always occurs after water has left the treatment plant when it travels through piping and plumbing containing lead. Water is naturally corrosive, and in some cases will corrode the pipes and plumbing through which it passes, picking up lead. This corrosion can occur in home fixtures as well.

To control the corrosion, and thus the lead in water, many public water systems add a corrosion inhibitor such as zinc orthophosphate to the water. While this is often effective as a means of corrosion control, it does have a downside, which is increased phosphate content in wastewater in that community.

NAWC has a number of recommendations to address the lead issue before this Subcommittee. Our recommendations closely follow those of the American Water Works Association, including the idea that EPA must rethink the "Silo" approach to regulation. Today rules are generally developed in isolation from one another, without consideration to the potential interconnectivity one rule may have with another. The recent experiences some communities have had with lead may be due to the drawbacks of the silo approach. We believe a holistic approach to drinking water regulation is needed that takes into account simultaneous compliance with existing drinking water and environmental regulations. In addition to this, NAWC recommends the following:

#### **1. NATIONAL LEAD REDUCTION STRATEGY.**

NAWC advocates a comprehensive approach to reducing lead contamination from all sources. Congress should require a respected body such as the Centers for Disease Control to complete a comprehensive study of lead exposure from all sources, and to develop a national strategy to reduce lead exposure from all significant sources. Such research should include a determination of the contribution to lead in drinking water from lead service lines, pipes inside the home, and plumbing fixtures.

NAWC also strongly advocates a continuing public education program concerning all sources and hazards of lead exposure and effective protective measures. Public education is a key component of a lead exposure reduction strategy. Water suppliers, working in cooperation with local and state public health officials and others, can help deliver the needed messages on the dangers of lead and the part everyone has to play in reducing risks. Since most lead contamination occurs inside the home from paint chips and dust or comes from home plumbing, increased public awareness is especially important.

## SMS EXHIBIT 2

**2. OPTIMIZATION OF CORROSION CONTROL.**

NAWC advocates the treatment technique of optimizing corrosion control as the best way of reducing exposure from lead in drinking water. Determining the corrosivity of water is complex and depended on several characteristics of the water. Lead contamination of drinking water is primarily the result of lead in home plumbing and fixtures beyond the control of a drinking water utility. The means available to drinking water systems to mitigate the degradation of water passing through pipes and fixtures in home plumbing is through implementation or modification of the corrosion control process. This can be done by adjusting the finished water's pH and alkalinity or by adding corrosion inhibitors.

If source water were the only way lead could enter drinking water, establishing a maximum contaminant level (MCL) for a utility to meet at the plant or in the distribution system would be sufficient to protect public health as it is for the majority of regulated contaminants. If lead were to occur in source waters, it could be removed in the treatment process. Public water systems are clearly responsible for and can control water quality at treatment facilities. However, the major source of lead in drinking water is not source water, it is lead from plumbing systems and faucets in homes that are beyond the control of drinking water utilities. The contribution of lead service lines to lead contamination is uncertain.

Some have suggested establishing an MCL for lead at the end user's tap. This would have the effect of holding water suppliers legally responsible not only for lead sources that they cannot control but also the mistakes, omissions, and even illegal activities of others. There is still lead solder in home plumbing although it was banned in 1986. Studies have shown that brass faucets holding lead free water for an eight-hour period can leach lead into water at levels of 10 ppb and higher. Grounding of electrical circuits in homes to water pipes and galvanic action between two dissimilar metals may increase corrosion that could cause lead to leach into the water. Customers who soften their water or otherwise change its corrosivity can affect the lead content of the water. These types of problems cannot be solved by an MCL at the tap or in the public water system. Each of these by themselves or in combination can cause lead to leach into drinking water. The SDWA limits EPA authority to regulating public water systems. A tap within a residence is not and should not be considered to be part of a public water system.

The SDWA also specifically prohibits USEPA from imposing both an MCL and a treatment technique for the same contaminant. Therefore NAWC advocates a lead control strategy of optimizing corrosion control in

## SMS EXHIBIT 2

conjunction with public education and a lead service line replacement program as the best method to protect public health.

### **3. REPLACEMENT OF LEAD SERVICE LINES.**

NAWC advocates lead service line removal as a means of reducing lead contamination in drinking water when the lead service line is significantly contributing to lead contamination. However, lead service line replacement is complicated by the ownership of the lines. In some instances, the water utility owns the entire line. In others, the property owner owns the entire service line. And in still other cases, part of the lead service line is owned by the utility and part by the property owner.

A public water system can only be held legally liable for replacing the service line or part of the service line owned by the utility. A public water system has no legal means to compel a property owner to replace a lead service line or portion of a lead service line. Requiring a water utility to remove privately owned lead service lines raises constitutional legal issues with regard to private property and eminent domain. All agree that partial replacement of a lead service increases lead levels in water and should be avoided. Further, removing a lead service line may not reduce lead contamination of drinking water. Tests have revealed high lead levels in homes that have no lead service line and low to no measurable lead contamination in homes with lead service lines. Removing lead service lines alone is not the complete solution to reducing lead exposure from drinking water.

Because of the costs involved and the likelihood there will be little or no public health benefit in some cases, lead service removal programs should focus on removing lead service lines owned by a utility that are significantly contributing to lead contamination as a high priority.

### **4. INDEPENDENT STUDY OF LEAD PROBLEMS AND LEGISLATIVE AND REGULATORY CHANGES.**

NAWC advocates an independent study of the drinking water lead contamination incidents to evaluate what if any changes may need to be made in the law or regulation. Based on recent USEPA data ([http://www.epa.gov/safewater/lcrmr/lead\\_data.html](http://www.epa.gov/safewater/lcrmr/lead_data.html)) there is no reason, at this time, to believe that there is a nationwide problem that would require changes to the SDWA. The current SDWA requirements protect public health and USEPA currently is engaged in an extensive national review of the Lead and Copper Rule implementation to identify how well the rule is performing across the nation and what gaps exist in federal guidance and regulation. The Lead and Copper

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Rule should not be revised until this review is completed.

NAWC recommends that Congress direct an independent study of the high lead levels in the District of Columbia water system be conducted. This could be done very soon in an appropriations bill.

### CONCLUSION

We appreciate the leadership role that this Subcommittee has taken to address water infrastructure problems, and we also appreciate the concern that you have expressed regarding the need for cost-effective solutions. These are long-term challenges, and we look forward to working with the Committee to achieve long-term solutions that will allow the drinking water industry to stand on its own two feet.



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## Indy Water P3 Pumps City's Rate Request

Operating cost savings produced by Veolia Water for Indianapolis are expected to help the city make a strong case to utility regulators this summer for a 30% increase in water rates.

According to the Indianapolis Dept. of Waterworks, its operating costs are lower now than when it bought the investor-owned system from NiSource and contracted out operations to Veolia four years ago.

"Because our operating costs are lower than when NiSource operated the utility, because we can take advantage of lower interest rates, and because we don't answer to shareholders, we have been able to keep rates frozen while continuing to invest in the system," says Carmen Hansen-Rivera, who chairs the board of the Indianapolis Dept. of Waterworks.

The revenue increase would be used to pay for a \$260-million, four-year capital program, most of which would be managed by Veolia as part of its capital plan for the municipally owned system. In addition to its O&M services, the company has directed about \$30 million a year of capital projects since 2002, charging a management fee of 7.5%.

Including its project management fee, Veolia was paid \$48.5 million in 2005, according to Carlton Curry, Director of

Contracts and Operations for the Dept. of Waterworks.

The city paid NiSource \$515 million for Indianapolis Water Co. (IWC) in 2002. NiSource, a utility holding company, had bought investor-owned IWC a few years earlier but was forced to divest to reduce debt.

Just before the purchase, the city awarded Veolia a 20-year management contract to run 11 surface water treatment plants, 31 pumping stations, 19 water storage tanks, 4,000 miles of water main and 32,000 fire hydrants in the Indianapolis metro region.

To build voter support for its takeover of IWC, the city elected to have water rates regulated by the Indiana Utility Regulatory Commission (IURC). Mayor Bart Peterson also committed to freezing water rates for five years, ending April 30, 2007.

IWC had gotten a 30% rate increase eight years ago and was seeking another 30% increase three years later when the city took over the private system and deferred the rate request.

The Waterworks board last month unanimously petitioned the IURC for a 30% increase in water charges, starting next May. Details of the rate request are expected to be filed on July 24. If approved, the Dept. of Waterworks's request

would add \$5 to the current average monthly residential rate of \$16.23, according to a department press release. That's about equal to the rise in the Consumer Price Index (CPI) since the last increase in 1998.

To save money on wastewater operations, the city had contracted out O&M of its regional wastewater plant and collection system to United Water in 1994. It decided to compete operation of its water system a few years later. After a fiercely fought competition among four contract operators (PWF 2/02, p. 1), Indianapolis awarded Veolia Water North America a \$665-million contract (present value over 20 years).

French-owned Veolia, teamed with Philadelphia Suburban, submitted a bid with a first-year price of \$35 million for the fixed-fee component, which represents about 75% of the total payment for operations. Annual inflation increases are capped at 2.5% until 2008 when rates are allowed to rise at 88.6% of the national CPI.

Incentive payments for up to 25% of the fixed fee can be earned for meeting all performance measurements (all or nothing) in each of 40 categories of service. Thus far, Veolia has earned from 88% to 92.5% of available performance fees. Annual payments for performance started at \$5.1 million for eight months of 2002 and have increased steadily to \$8 million last year, says Curry.

Veolia's bid price in 2002 included the cost of a two-year job guarantee for all 471 of IWC's employees and of funding about \$2 million per year in medical benefits for 308 retired workers.

Yet Veolia still reduced operating costs, says Joseph Burgess, president of Veolia Water North America. He attributes that to the efficiencies that come from contract operations. "We've been able to take advantage of a large efficiency gap that we can work off of," he told a water conference in New York City last month.

The long term of the agreement also helped the city keep its promise on rates and helps Veolia recoup its early losses, says Curry. "We knew they'd probably lose money for the first four or five years and we wanted to give them a decade or so to get well," he says.

Veolia Water and United Water are likely to go head-to-head again in a competition this summer for renewal of the wastewater service contract, currently held by United Water. The Indianapolis Department of Public Works is seeking expressions of interest by July 28 and plans to issue an RFP by year end. Its RFEI did not specify a term for the new contract.

Also in play are long-term operating contracts held by United Water for wastewater systems that come up for renewal in Milwaukee next year and in Gary, Ind., in 2008.

### INDIANAPOLIS 1994 WASTEWATER CONTRACT SNAPSHOT

- > Procurement Advisor: Camp, Dresser & McKee
- > 10-yr contract signed with United Water 3/94 for two AWT plants (250 mgd) plus storm/sanitary sewer system. First-year fee: \$22.5 million. 272,000 connections serving 1.3m people
- > Operator: White River Environmental Partnership (WREP): IWC Resources (Indianapolis Water Co.), Suez Lyonnaise des Eaux, United Water Services, plus AFSCME local union
- > Negotiated 10-yr extension early 1998 to combine treatment plant/collection system OM&M contracts. Estimated combined savings, \$189 million

### ■ Glens Falls, NY Defaults Earth Tech

A new city administration in Glens Falls, N.Y., on June 5 cancelled Earth Tech's utility operations contract due, in part, to a dispute over who's responsible for the company's failure to pay prevailing wages for pipe laying work done under the city's collective bargaining agreement.

Earth Tech was paid \$3 million in 2005 under its 20-year contract to operate and maintain the city's wastewater treatment plant and collection system, stormwater collection, and water distribution system.

A New York state Dept. of Labor (DoL) audit last August reportedly found that Earth Tech owed

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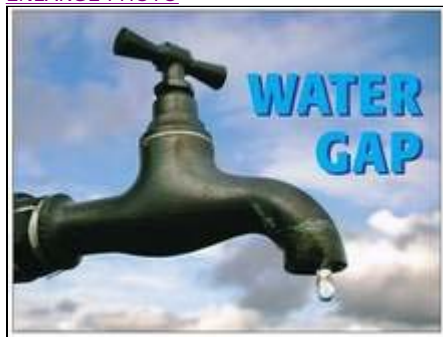
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## State survey finds higher rates among for-profit companies

By [Bob Sanders](#)

Published: Friday, Apr. 29, 2005

[ENLARGE PHOTO](#)

Private water companies in New Hampshire generally have higher rates than their public counterparts and their rates are going up at a faster rate — according to a New Hampshire Business Review analysis of a state survey of water rates.

The survey shows that privately held Pennichuck Water Works has the highest rates of any system serving more than 25,000 people. The Merrimack-based firm's rates doubled in a decade and have climbed 53.8

percent in the last three years. By contrast, the rates among the seven other largest systems rose 38 percent, while the average increase of water rates among all state water companies increased less than 15 percent over the last three years.

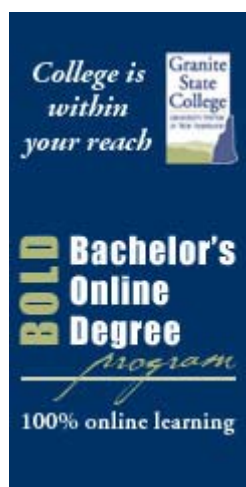
The figures were culled from a rate survey — scheduled to be released in its entirety next month — that is conducted periodically by the Department of Environmental Services. It may not be welcome information to Pennichuck Water Works' parent company, Pennichuck Corp., which currently is fighting a proposed eminent domain takeover of its water systems by a municipal consortium led by the city of Nashua.

Pennichuck is currently asking the state Public Utilities Commission for another 11 percent increase on top of the 8 percent temporary increase it received last year.

Pennichuck's rates were only \$10 above the state average in 2004, which was \$350-a-year based on residential usage of 275 gallons per day. (Actual typical usage varies geographically, but DES selected such a standard usage for rate comparison purposes.)

However, "rates are usually lower with larger systems, because the base rate is spread out over a larger number of rate payers," said Richard Skarinka, the DES engineer in charge of the survey.

## SMS EXHIBIT 4



Pennichuck officials agreed, but argued that the company – the second largest system of the state – serves a number of smaller municipalities, several of which are scattered throughout the state as well as Nashua. Thus, they argue, Pennichuck's rates are not really comparable with water utilities that just serve one city and perhaps a surrounding area.

In addition, some of these smaller systems were "basket cases" before Pennichuck took them over, said Don Ware, senior vice president of operations at Pennichuck.

That led the utility to invest in the acquisition's infrastructure, which was partly subsidized by Nashua ratepayers, Ware said.

Such investments are one of the reasons Pennichuck's rates have gone up, Ware explained. Municipal officials have to face the voters every few years and are reluctant to spend the money needed to maintain a system, he argued.



"We have kept on top of aging infrastructure that most communities ignore," said Ware. "That's why our rates have gone up. We have stepped to the plate and attempted to keep up with improvements."

Larry Bingaman senior vice president of Aquarion Water Company of New Hampshire, which runs the Hampton Water Works System, echoes that view.



"The rates generally reflect how much is invested in the system," said Bingaman, who cites national studies that show that public water systems don't invest enough.

#### NETWORK PARTNERS



### State averages

Keeping up with infrastructure maintenance is the very reason Manchester Water Works cites for its rates, which are less than two-thirds that of Pennichuck.

"Manchester probably took a long look at investing in preventative maintenance than many other systems, so we have a better maintained system," said Tom Bowen, director of Manchester Water Works.

Manchester's water rates have increased slightly more than half as much as Pennichuck's during the last three years.

That's not to say that the Queen City hasn't seen an increase in water rates. Manchester is in the midst of a four-year increase that started in 2002 to pay off bonds for a new water treatment plant. Before that, the last increase in Manchester's rates was in 1991.

Higher rates are not limited to Pennichuck. The rates of other private water companies tend to be higher than their counterparts. The rates of Aquarion Water Company of New Hampshire, which serves the Hampton area, were \$453 (based on the standard average usage), far higher than the average for a system that size. The Tilton-Northfield Aqueduct Company — at \$712 — is one of the highest in the state. Water users in the towns of Tilton and Northfield have recently voted to acquire that system.

Pennichuck's other systems serving such communities as Pittsfield and Pelham — outside the core of the Nashua-based water works — also have rates far higher than the state average.

## SMS EXHIBIT 4

Indeed, the only private water system serving a municipality whose rates are comparatively low is Hanover Water Works, a utility that is managed by the town itself.

Some public municipal water systems also have higher-than-average rates. Berlin's, for instance, is a whopping \$714 — the highest-priced larger system in the state — and Rochester is at \$450 and Dover at \$358.

Dover's rates might be higher because it has a flat rate for usage: no differences between commercial and residential rates nor cheaper rates for big users, said Jeff Harrington, Dover's finance director. But these tend to be the exception to the rule.

One reason municipalities have lower rates is that they don't have to pay property taxes. Pennichuck, for instance, pays \$1.1 million in property taxes in its core area, according to Bonnie Hartley, vice president of administration at Pennichuck.

"If we didn't pay it, somebody else would," she said. In other words, whatever a ratepayer may save in his or her water bill, would be offset by a higher property tax bill, she said.

The other major difference is that private companies are entitled to a profit. Nashua attorneys have argued before the Public Utilities Commission that if some of that money that goes to shareholders and other private ventures were plowed back into the infrastructure, rates — in the long run — would go down.

Other Pennichuck critics echo that view.

"No matter how you cut the numbers, you take stockholders' profits out of the equation, it will be cheaper for ratepayers," said state Rep. Mary Ellen Martin

Ware, however, argued that too much is made of the profit that goes into shareholders' pockets, comparing it to the interest that municipalities pay on the debt for capital improvement on the systems. Profits do amount to more, Ware admitted, but only by a slight amount.

It isn't profits but efficiency that most private companies tout when comparing themselves to municipal systems.

"Profit is what drives private companies to be more efficient," said Bingaman of Aquarion. "Studies show that private investor water companies have fewer employees and are more efficient."

However, according to Hudson Town Administrator Steve Malizia, private companies can be inefficient as well. Hudson took over its water works from the Consumer NH Water Company in 1998 because its rates were among the highest in the state, and it was poised for another 30 percent increase, Malizia said.

The reason, said Malizia, was that the company made a number of poor management decisions, spending hundreds of thousands of dollars to expand the system for only a few customers. The town bought the system, cut the rates by 10 percent, and while rates were still very high — \$571 based on standard usage — they haven't gone up since.

Malizia blames the high rates on the debt service on the purchase, which includes paying for some of the mistakes the company made in the past.

Hudson is now watching with interest the battle between Pennichuck and its neighbor to the east. The town doesn't take sides. Indeed it hires Pennichuck to

## SMS EXHIBIT 4

take care of its wells. And so far nobody, including those on both sides of the dispute, has approached the town to discuss its experience in going from a private water supplier to a publicly owned one.

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City of Nashua Petition for Valuation Pursuant to RSA 38:9

DW 04-048

Staff's Response to the City of Nashua's Sixth Set of Data Requests

Date of Request: April 27, 2006  
Data Request No.: Nashua 6-46

Date of Response: May 18, 2006  
Witness: Mark A. Naylor

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REQUEST: Please identify and list all "troubled systems" acquired by any other investor owned water utility in New Hampshire and state the date of such acquisition, the number of customers and the Docket number of the Commission under which each acquisition was approved.

RESPONSE:

By Lakes Region Water Company:

Brake Hill Acres, DE 94-187, Order No. 21,475 (December 22, 1994)  
Deer Cove, DW 04-031, Order No. 24,376 (September 30, 2004)  
LOV Water, DW 04-031, Order No. 24,376 (September 30, 2004)  
Gunstock Glen, DW 05-097, Order No. 24,519 (September 22, 2005)  
Indian Mound Water, DW 04-090, Order No. 24,374 (September 23, 2004)  
Echo Lake Woods, DF 90-152, Order No. 20,144 (June 5, 1991)  
Tamworth Water Works, DE 95-323, Order No. 21,943 (December 12, 1995)  
Hidden Valley, DW 01-217, Order No. 23,930 (March 8, 2002)

By Integrated Water/Central Water:

Locke Lake, DE 93-084, Order No. 20,865 (June 10, 1993)

By Integrated Water/Consolidated Water:

Indian Mound Water, DE 95-331, Order No. 22,203 (June 18, 1996)

By Southern NH Water Co.:

Policy Water Systems, DE 85-354, Order No. 18,010 (December 19, 1985)  
Springwood Hills, DE 93-203, Order No. 21,219 (May 10, 1994)

By Hampstead Area Water Company:

Colby Corner, etc., DE 89-047, Order No. 19,751 (March 9, 1990)

## SMS EXHIBIT 5

By Hudson Water Company:

Williamsburg Water Company, DE 78-235 & DE 79-134, Order No. 13,781 (August 13, 1979)

By Lower Bartlett Water Precinct:

Holiday Ridge, DE 96-257, Order No. 22,581 (May 1, 1997)

Birchview by the Saco, DW 97-255, Order No. 23,253 (July 7, 1999)



## SMS EXHIBIT 6

## Pennichuck Corp

PNNW 18.30 ◆ NA ◆ NA

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## Tab keystatistics:

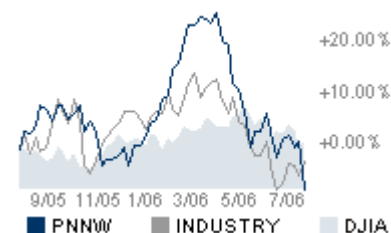
## PNNW PENNICHUCK CORPORATION

Industry: **Water Utilities** Exchange: **NASD** Compare(New!)

Volume: NA Avg Volume: 4,700  
 52-wk High: \$25.90 52-wk Low: \$18.02  
 Day's High: NA Day's Low: NA  
 Dividend: \$0.17 Yield: 3.61%  
 Market Cap (thousands): 77,000 P/E (Forward): 49.46

18.30

▲ NA (NA)

Last Trade  
NA  
NA

After-Hours Trading:

Last Trade: **NA**Price: **NA**Volume: **NA**

## Key Statistics | Compare(New!)

TTM as of 3/31/2006	Total*	Per Share**
Revenues	\$24,041	\$5.74
Income from Continuing Operations	\$231	\$0.06
EBIT	\$2,325	\$0.55
Ebitda	\$8,154	\$1.95
Net Income	\$231	\$0.06
Cash Flow from Cont. Ops	\$5,120	\$1.22
Free Cash Flow	\$-5,762	\$-1.37
Cash	\$611	\$0.15
Long-Term Debt	\$40,940	\$9.77
Book Value	\$44,360	\$10.58
Enterprise Value	\$117,840	\$28.12
Market Capitalization	\$77,005	\$18.37

\*Figures in thousands

\*\*Based on most recent share count

## Share Liquidity &amp; Volatility | Compare(New!)

Beta	0.07
Liquidity Ratio	85
Float	4,149,413
Shares Outstanding, Basic	4,208,000
Shares Outstanding, Diluted	4,191,273
Float as a % of Shares Out	98.60%

## Profitability &amp; Efficiency | Compare(New!)

TTM as of 3/31/2006	
Gross Margin	33.92%
Operating Margin	NA
Net Margin	0.96%
Return on Common Equity	0.56%
Return on Invested Capital	0.29%
Return on Assets	0.19%
Inventory Turnover	32.53
Asset Turnover	0.19

## Valuation | Compare(New!)

P/E (GAAP, TTM as of 3/31/2006)

261.43

## Financial Strength | Compare(New!)

Current Ratio

4.80

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P/E (Pro Forma, TTM as of 3/31/2006)	289.20	Quick Ratio	4.63
Forward P/E (as of 7/19/2006)	49.46	Interest Coverage	-0.99
PEG	6.18	Long-Term Debt/Equity	0.92
Price-to-Book	1.74	Total Debt/Equity	0.93
Price-to-Sales	3.19	Long-Term Debt/Total Capital	0.48
	Low	High	Average
5-Year P/E	12.80	360.00	58.70

**Stock Performance & Dividends** | Compare Dividends(New!)

	YTD	52-Week	3-Year	5-Year
Share Price	-10.51%	-8.04%	1.05%	2.46%
Dividends (Yield)			\$0.17 (3.61%)	
Dividend Growth (5 years)			\$3.49	
Dividend Payout			\$9.71	
Dividend X-Date			5/11/2006	

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## PNNW PENNICHUCK CORPORATION

18.30

▲ NA (NA)

Industry: **Water Utilities** Exchange: **NASD**

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### Glossary A-E

[ABCDE](#) [FGHIJK](#) [LMNOP](#) [Q](#)

#### Additional Paid-In Capital

Capital received from investors in exchange for stock, as distinguished from capital generated from operations.

#### Address

The headquarters address of the company as provided in the latest 10-Q or 10-K SEC forms or news.

#### After-Hours Last Trade Volume

The total number of shares of a stock exchanged in the last reported [after-hours trade](#).

#### After-Hours Price

The price per share of the last reported [after-hours trade](#).

#### After-Hours Trade

A stock trade that takes place after the regular trading session closes. See [extended-hours trading](#).

#### Amortization

The repayment of a loan by installments.

#### Asset Turnover

The ratio at which each dollar of assets has generated a dollar in revenues, calculated by dividing the quarters' [revenues](#) by the average of the past four quarters' [total assets](#). Also called asset turns.

#### Average Volume

Total volume for the previous three months, divided by the number of trading days of the previous three months, and then divided this number to the daily [volume](#) to see if investor interest in the stock has increased or decreased.

#### Barra Risk Factor

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FISHER INVESTMENTS

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Markets	Top 10 Movers
DJIA	11011.42 ▲ <b>212.19</b>
Nasdaq	2080.71 ▲ <b>37.49</b>
S&P 500	1259.81 ▲ <b>22.95</b>
Rus 2000	702.34 ▲ <b>20.70</b>
10 Yr Bd	5.07 ▲ <b>0.02</b>
DJTA	4695.09 ▲ <b>92.82</b>
Wil 5000	12663.34 ▲ <b>244.90</b>
S&P 400	740.22 ▲ <b>17.49</b>
Nas 100	1490.60 ▲ <b>18.26</b>



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Measures a stock's predicted risk relative to the overall market, to its sector and to its industry. Barra analysis on 40 different data items, including market information (things such as dividend yield, market fundamental measures (earnings, sales, assets) and technical indicators (relative strength, standard deviation, turnover).

The resulting number indicates the percentage of stocks that are less risky than the stock being assessed; number, in other words, the less risk. For example, a company with a Risk Factor of 14, a sector Risk Factor of 7 would be riskier than just 14% of Barra's universe of more than 6,200 stocks in its sector and riskier than 7% of stocks in its industry.

[Beta](#) is often used as a gauge of risk, but it has limitations. It looks only at price performance, not at profitability, and thus is more a measure of volatility than risk. Plus, it's based on *past* volatility, so it often grows with companies that have recently become profitable, and more stable. Barra Risk Analysis, then, is a more comprehensive measure of actual risk than beta.

### Beta

A measure of share-price volatility. Beta is calculated using a statistical technique called regression analysis of the historical relationship between variables to predict their future relationship. SmartMoney.com beta is based on 36-month regressions vs. the Standard & Poor's 500 index. The index is assigned a beta of 1.0. A stock would be said to exhibit 50% more volatility than the index, meaning that if the index rises (or falls) 8% it is expected to rise (or fall) 12%. A stock with a beta of 0.8 would be 80% as volatile. One with a negative beta would be negatively correlated--it would be projected to "zig" when the market "zags."

Beta is often thought of as a measure of risk, although strictly speaking, it's not. For one thing, it says nothing about financial risk to the extent that risk is not exhibited in share price movements. Also, it's based on the past and thus punishes young companies that have become more stable over the past three years. Alternatives to the "bottom-up" betas, such as the [Barra Risk Factor](#), which are calculated using fundamental data rather than price movements.

### Book Value

The difference between a company's total assets and total liabilities, as reported on its most recent balance sheet. [shareholder's equity](#).

### Cash and Equivalents

On-hand currency, bank balances and bullion (not counted for mining companies) as reported on a company's quarterly balance sheet.

### Cash Flow

[Net earnings](#) before [depreciation](#), amortization and non-cash charges. Sometimes called cash earnings, it is calculated by adding depreciation to net earnings and subtracting preferred dividends. It is useful for determining a company's ability to pay dividends.

### Chief Executive Officer (CEO)

The highest ranking executive who manages the day-to-day operations of the firm, updated according to the company's annual report or newswire announcement.

### Common Equity

This is the amount of [shareholders' equity](#) attributable to common stock. Common stock equity generally consists of the following items: common stock at par value, capital surplus and retained earnings.

### Common Stock Equity

The amount of [stockholders' equity](#) attributable to common stock. Common stock equity generally consists of the following items:

1. Common stock (all issues) at par value.
2. Capital surplus or [additional paid-in capital](#).
3. [Retained earnings](#) or earned surplus (net of foreign exchange gains/losses).

## SMS EXHIBIT 6

**Consensus Earnings Estimate**

The average of analysts' per-share earnings forecasts for the indicated period.

**Cost of Sales**

All expenses directly associated with the production of goods or services a company sells (such as m excluding [depreciation](#), [depletion](#), [amortization](#) and SG&A.

Typical accounts: cost of goods sold, materials and production expenses, gas purchased, fuel and po exploration and well drilling expense, mining expense and oil and gas property abandonments.

**Current Assets**

Assets that can be converted to cash within a relatively short period of time, usually 12 months. These [equivalents](#), [receivables](#), [inventories](#) and [other current assets](#).

**Current Liabilities**

Obligations that must be paid within 12 months. These include accounts payable, short-term debt and [debt](#).

**Current Ratio**

A measure of a company's abilities to meet its short-term obligations, calculated by dividing its total [c](#) [current liabilities](#), as found on its most recent quarterly balance sheet.

**Current Share Price**

Most recent market price of the shares. Our quote feed is on a 20-minute delay.

**Day High**

The high price of the last trading day.

**Day Low**

The low price of the last trading day.

**Debt/Total Capital**

This ratio indicates how much financial leverage a company has. It is calculated by dividing total debt Total debt is long- and short-term debt obligations, including bonds, notes payable, mortgages, lease industrial revenue bonds. Total invested capital is the sum of common and preferred stock equity, lon income taxes, investment credits, and minority interest.

**Depletion**

The using up of an asset. Items which can be physically reduced, like the output of coal mines, are ac depletion rather than [depreciation](#).

**Depreciation (and Amortization)**

A non-cash charge that represents a reduction in the value of fixed assets due to wear, age or obsole includes [amortization](#) of leased property, [intangibles](#) and [goodwill](#), and [depletion](#).

**Dividends**

Cash payments made to a company's shareholders from its current or retained earnings. If a compan to dividend payments in the future, the latest reported dividend rate equals the number of times the cc per year times the latest dividend, expressed in dollars. If a company's board has not committed to di future, the latest reported dividend rate equals the total dividends paid in the past 12 months.

Dividends are typically paid by mature companies whose growth rates have slowed, and which no lon of their earnings. The payments are taxable to shareholders as income.

## SMS EXHIBIT 6

**Earnings Per Share**

Net earnings divided by common shares outstanding. May be [diluted](#) to account for the potential creation of new shares from convertible securities. See [earnings per share, diluted](#).

**Earnings Per Share, Diluted**

Net earnings divided by common shares outstanding, adjusted for the assumed conversion of all potential common shares into common stock. Securities having a dilutive effect may include convertible debentures, warrants, and convertible preferred stock.

**Ebit**

Earnings before deductions for interest and taxes. Also called [operating income](#).

**EBITDA**

Earnings before interest, taxes, depreciation and amortization. Roughly equal to [operating cash flow](#), income statement, rather than the cash flow statement.

Ebitda is useful for evaluating companies that are subject to large [depreciation](#) charges for their fixed assets. Companies with significant amounts of [goodwill](#) that they must amortize. Such charges would normally distort a company's earnings power; Ebitda is designed to gauge operational cash flow by excluding these items. The measure is useful for evaluating companies that have low earnings because of large restructuring, capital build-out or acquisition.

**Enterprise Value**

Total purchase price of a company, net of its debt and cash. Equal to market capitalization (share price times shares outstanding) plus long- and short-term debt and preferred stock, minus cash. Commonly used in acquisition analysis.

**EPS**

See [earnings per share](#).

**Estimated EPS Growth**

The mean estimate of [earnings-per-share](#) growth (for the indicated period) as derived from all polled analyst estimates. This information is provided by Zacks Investment Research.

**Extended-Hours Trading**

Nasdaq can now transact "after-hours" trades. These are trades that take place after the regular market hours until 6:30 p.m. ET. There is also a "premarket window" permitting Nasdaq trades before the regular market hours at 9:30 a.m. ET. These trades can take place as early as 8.00 a.m. ET.

Trades outside of regular trading hours are classified as "Form-T" trades. Form-T trades don't impact closing prices, but are reckoned in [volume](#) reporting. Nasdaq has specified that the "closing quote" of the regular trading hours is identified separately from extended-trading-hours quotes.

[ABCDE](#) [FGHIJK](#) [LMNOP](#) [Q](#)

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City of Nashua

*Petition for Valuation Pursuant to RSA 38:9*

DW 04-048

Nashua's Responses to Pennichuck Water Works, Inc. Data Requests – Set 5

Date Request Received: June 1, 2006

Date of Response: June 22, 2006

Request No. 5-9

Respondents: Mayor Streeter,  
President Rootovich, Alderman McCarthy.

---

Req. 5-9      On page 11 of your testimony, you refer to “high cost of service systems” in Newmarket and Epping. Please define “high cost of service systems” and explain specifically what makes systems in Epping and Newmarket high cost systems, and explain whether you believe that these systems are more or less costly to operate than the Nashua core system. Identify all documents which support your answer.

ANSWER:      We referred to these systems as high cost of service systems because they are located outside of Pennichuck's core service area, have relatively few customers. We believe that their cost of service per customer is higher than the core system as reflected in statements made by Pennichuck Water Works employees, the Commission staff and in the testimony of George E. Sansoucy, P.E.

By way of example:

In Order No. 22,883, Staff economist James Lenihan noted that “the “subsidy” by core customers, although small, would be inappropriate.” The Commission approved a single rate of \$253, even though the cost of service for the stand alone systems would require “annual rates in the range of \$800 to \$1200”.

In an April 29, 2005 article in the New Hampshire Business Review, Donald Ware stated that Pennichuck's rates were higher than expected because Pennichuck “serves a number of smaller municipalities, several of which are scattered throughout the state”, that “some of these systems were ‘basket cases’ before Pennichuck took them over” and that these systems were “partly subsidized by Nashua ratepayers.”

According to the 1998 NH PUC Order approving the acquisition of the Great Bay Water Company in Newmarket, Order No. 23,044, the system acquired in Newmarket serves 87 customers and Pennichuck's rates averaged \$212 per customer per year at the time the acquisition was approved. This results in an annual revenues of only \$18,444.



City of Nashua

*Petition for Valuation Pursuant to RSA 38:9*

DW 04-048

Nashua's Responses to Pennichuck Water Works, Inc. Data Requests – Set 5

Date Request Received: June 1, 2006

Date of Response: June 22, 2006

Request No. 5-10

Respondents: Mayor Streeter,  
President Rootovich, Alderman McCarthy.

---

Req. 5-10      On what basis does Nashua claim that the rates of the PWW core customers are funding the acquisition of additional community water systems? Please explain the rate recovery mechanism that you believe PWW is using to fund these acquisitions and identify every such acquisition and the amount of rate relief you alleged PWW obtained from the Public Utilities Commission to fund the acquisition.

ANSWER:      We believe that Pennichuck deferred investment in its core system in order to use revenues from operation of its core system in order to acquire satellite systems. The addition of satellite systems, increased maintenance costs due to deferred maintenance or capital projects are largely paid for by customers of the core system.

One example of deferred maintenance is contained in the May 22, 2006 Reply Testimony of Veolia Water North America:

It is clear from the NHPUC annual reports that PWW has not made the required investments in replacing existing underground infrastructure. As indicated in the 2004 annual report to the NHPUC PWW's system had over 232,000 feet of asbestos cement pipe and over 838,000 feet of older cast iron pipe. The Northeast LLC will work with the City of Nashua to ensure that the older cast iron pipe with high failure rates and asbestos cement pipe will be targeted for replacement. Over the next ten years Nashua will have no choice but to make major investments in replacing and rehabilitating pipes.<sup>3</sup>

This is one example where the company has deferred major capital investment into the core system in order to focus on satellite acquisitions. Capital invested into satellite acquisitions is unlikely to add sufficient new revenue to offset revenue requirements and exacerbate the need for a rate

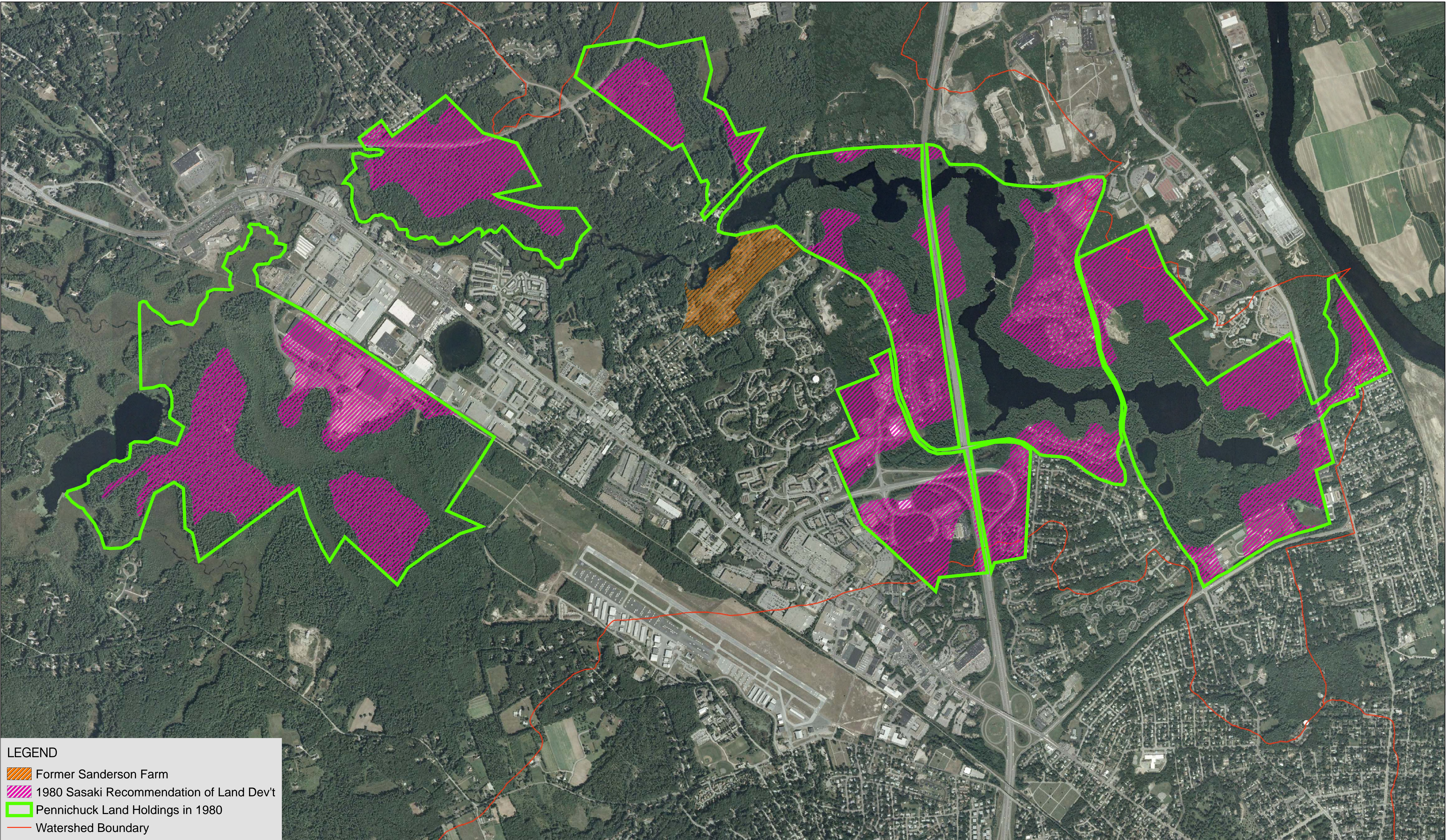
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<sup>3</sup> See e.g. May 22, 2006 Reply Testimony of Philip Ashcroft et al., Page 14, Lines 16 to 23.

increase. As a result, when the deferred replacement of cast iron and asbestos cement pipe is completed customers face higher rates than they would have faced without the satellite acquisitions.

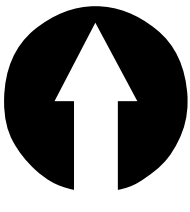
We do not, however, oppose the acquisition of all satellite systems. As we have noted elsewhere in our testimony and in responses to data requests, we believe that water systems acquisitions by Pennichuck Water Works, or operated using its staff and/or assets should be focused, Inc., should focus on the lower Merrimack River watershed.





LEGEND

-  Former Sanderson Farm
-  1980 Sasaki Recommendation of Land Dev't
-  Pennichuck Land Holdings in 1980
-  Watershed Boundary



0

900

Feet

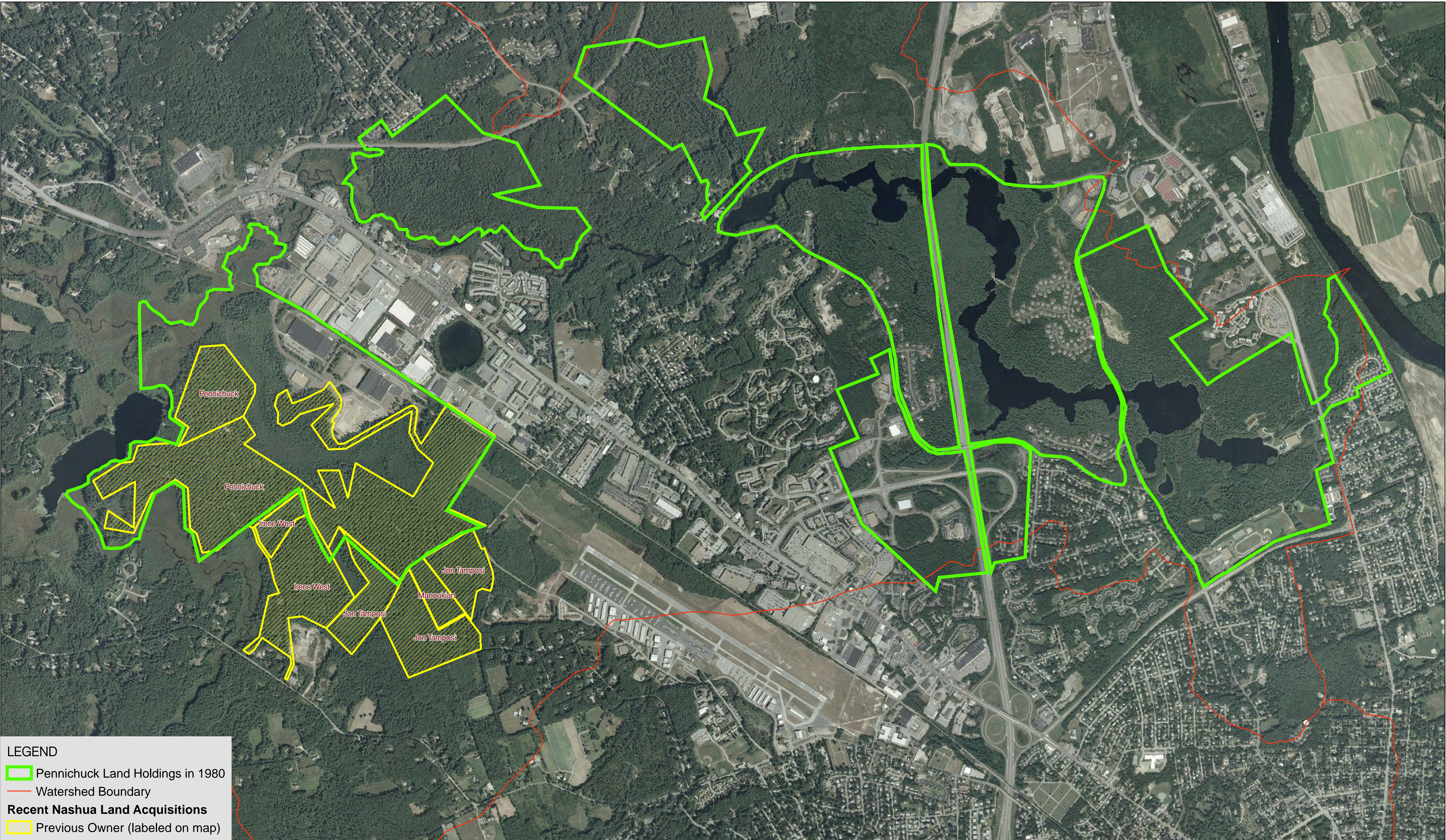
1 inch equals 900 feet

Source: NAIP 2003 Orthophotos, Sasaki Associates Report

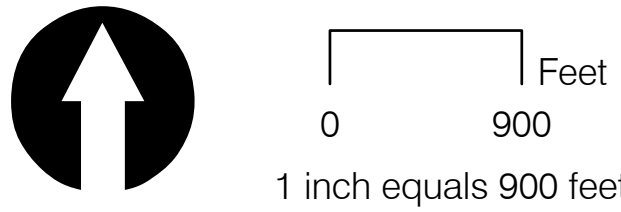
**RIZZO**  
ASSOCIATES  
A TETRA TECH COMPANY

Pennichuck Water Works Land Holdings  
Then and Now





Conservation Land in Pennichuck Brook



Source: NAIP 2003 Orthophotos, Sasaki Associates Report