STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

RE: PENNICHUCK EAST UTILITY, INC.

DOCKET NO. DW 09-___

PETITION FOR AUTHORITY
TO ISSUE UP TO $6,000,000 OF LONG TERM DEBT

Pennichuck East Utility, Inc. ("PEU") or the ("Company") hereby petitions the Public Utilities Commission for authority, pursuant to RSA 369:1 and Puc 609.03, to issue up to $6 million in long-term debt, and in support of its request states as follows:

1. PEU is a New Hampshire corporation, authorized by this Commission to provide water service to customers in various communities in southern New Hampshire.

2. As described in the pre-filed direct testimony of Thomas C. Leonard, which accompanies this petition, PEU currently has a 10 year, $4.5 million floating-rate secured note payable to Bank of America that matures on December 31, 2009, which it intends to refinance. PEU is also currently undertaking certain on-going capital improvements to its facilities and desires to repay certain short term intercompany borrowings.

3. PEU intends to borrow up to $6 million in notes with a 20 year term, from CoBank, ACB ("CoBank"), to refinance its existing $4.5 million debt owed to Bank of America, finance a portion of the funds required for its ongoing capital improvements, and repay existing short term intercompany borrowings.

4. The 20-year, $6 million loan will have an interest rate not expected to exceed 6 to 6.5%, subject to completion of due diligence by CoBank.

5. CoBank is a Government Sponsored Enterprise owned by its customers, which issues debt with the implicit full faith and credit of the U.S. Government. CoBank's borrowing costs are lower than commercial banks and financial institutions, and the benefit of these lower costs are passed on to its borrowers. Each year CoBank's Board of Directors targets a refund amount that is returned to borrowers based on the annual average accruing loan volume. These "patronage payments," although not guaranteed, are an additional expected benefit related to the financings with CoBank. *See* pre-filed direct testimony of Thomas C. Leonard submitted in support of this petition. Mr. Leonard's testimony also addresses the filing requirements of Puc 609.03.

6. The financings being proposed by PEU are in the public interest and consistent with the public good because they will enhance PEU's ability to provide safe drinking water to its customers on a reliable basis at a reasonable cost.

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

A. Authorize PEU to borrow up to $6 million in long term debt from CoBank, ACB to refinance its 10 year, $4.5 million floating-rate secured note payable to Bank of America, which matures on December 31, 2009, and to finance an additional $1.5 million for on-going capital improvements and the repayment of existing short term intercompany borrowings, as described in this Petition and the pre-filed testimony of Thomas C. Leonard;

B. Find that the issuance of one or more promissory notes and the execution and delivery of related documents by PEU for purposes of consummating the aforesaid financings are consistent with the public good;

C Find that the uses of the proceeds from the proposed financings are prudent and consistent with the public interest;

D. Issue an Order Nisi authorizing PEU to borrow up to $6 million in long term debt from CoBank, ACB in accordance with the terms and conditions set forth above and as otherwise provided by CoBank, ACB; and

F. Grant such other and further relief as may be just and reasonable.

Respectfully submitted,

PENNICHUCK WATER WORKS, INC.

By its Attorneys,

McLANE, GRAF, RAULERSON & MIDDLETON,
PROFESSIONAL ASSOCIATION

Date: July 27, 2009

By: Julie Richardson, for

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Certificate of Service

I hereby certify that a copy of the foregoing Petition has been forwarded this 27th day of July, 2009 to Meredith Hatfield, Esq. of the Office of the Consumer Advocate.

Julie Richardson, for
Sarah B. Knowlton

STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

Re: Pennichuck East Utility, Inc. –

Debt Financing

DW 09-

DIRECT PREFILED TESTIMONY OF THOMAS C. LEONARD

July 27, 2009

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

A. My name is Thomas C. Leonard. I am the Chief Financial Officer of Pennichuck East Utility, Inc. ("PEU" or the "Company"). I have been employed with the Company since July, 2008. I serve as Senior Vice President, Treasurer, and Chief Financial Officer of Pennichuck Corporation ("Pennichuck"), the parent company of PEU. I am a licensed Certified Public Accountant in Massachusetts.

Q. Please describe your educational background.

A. I have a Bachelor's degree in Business Administration--Accounting from the University of Wisconsin in Madison, Wisconsin.

Q. Please describe your professional background.

A. Prior to joining the Company, I was a Vice President with CRA International from June, 2006 to May 2008 and before that a Managing Director with Huron Consulting Group from December 2002 to May 2006. My role at both organizations was to provide expert accounting and financial analysis and testimony in connection with investigations and disputes. Prior to joining Huron, I was the Head of the Audit Division in New England for Arthur Andersen LLP and served as Audit Partner for a wide range of clients including water, gas and electric utilities.

Q. What are your responsibilities as Chief Financial Officer of the Company?

A. As Chief Financial Officer of the Company I am responsible for the overall financial management of the Company including financing, accounting, and budgeting. My responsibilities include the issuance and repayment of debt, issuance of common or other forms of equity, as well as quarterly and annual financial reporting. I work with the President of PEU to determine the lowest cost alternatives available to fund the capital requirements of PEU that result from PEU's annual capital expenditures and its current debt maturities.

Q. Please provide the Commission with an explanation of the purpose of the financing proposed by the Company in its petition in this proceeding (the "Proposed Financing").

A. The primary purpose of the Proposed Financing is to refinance a 10 year, $4.5 million floating-rate secured note payable to Bank of America that matures on December 31, 2009. The Company also plans to borrow an additional $1.5 million to fund its on-going capital improvement program and repay short term (intercompany) borrowings from Pennichuck.

I will note that PEU will also be establishing a borrowing line of up to $1.5 million to provide borrowing capacity at PEU to fund future capital expenditures including acquisitions if and when they arise. This independent PEU borrowing line will reduce PEU's need to rely on its parent company, Pennichuck, for its short term liquidity needs and, thus, help mitigate the risk that short term financing at its parent could be curtailed in the event the eminent domain taking of Pennichuck Water Works is consummated.

Q. Please describe the debt that PEU is seeking authority to incur.

A. PEU is seeking authority to borrow $6.0 million from CoBank, ACB ("CoBank"). CoBank is a federally chartered bank under the Farm Credit Act of 1971, as amended. Unlike commercial banks and other financial institutions, it is restricted to making loans and leases and providing financial solutions to eligible borrowers in the agribusiness and rural utility industries and certain related entities as defined under the Farm Credit Act of 1971. The characteristics of PEU's service territory are consistent with CoBank's charter and mission and it can therefore provide short, intermediate, and long-term loans to PEU in connection with its capital requirements.

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

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

A. While the final terms and interest rates are subject to change based on CoBank's due diligence (which is in progress) and market conditions, PEU expects to obtain $6 million in notes payable with a 20 year amortization period that would replace the $4.5 million secured note payable and certain intercompany borrowings. The Company's objective is to obtain the longest term available on a cost effective basis in order to match the debt amortization payments with the recovery of the cost of the assets via the depreciation expense. Based on current market conditions, a significant market premium exists for longer term debt. In fact, Bank of America, the holder of the $4.5 million note due at December 31, 2009, has indicated that will not generally write new long term loans with a life in excess of 7 years. By contrast, CoBank has indicated an expected borrowing rate for a 20 year amortizing loan to be in the range of 6-6.5%.

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

A. Yes, as I mentioned earlier in my testimony, CoBank is organized as a cooperative which means it is owned and controlled by its members who use its products or services (i.e. its borrowers). A key cooperative principle is the return to customers of a portion of net margins based upon their use of the bank. This is accomplished through "patronage refunds"---the refunding to patronage customers of net margins remaining after payment of preferred stock dividends, deducting operating and interest expenses and amounts retained as core surplus. While not guaranteed, each year the Board of Directors of CoBank targets a refund amount which is returned (in the subsequent year) to its borrower/members based on the annual average accruing loan volume. While these "patronage" payments are not guaranteed and therefore are not included in the pro forma cost of capital on Exhibit TCL-3, the Company expects to reflect them in rates in future test years based on the receipt of the payments.

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

A. The anticipated issuance costs total $15,000 and relate primarily to legal costs which will be incurred to (i) review and revise the necessary loan documentation prepared by the bank and (ii) obtain Commission approval of the loans. The issuance costs will be amortized over the twenty-year life of the CoBank loan. The annual amortization expense of less than $1000 associated with the issuance costs has not been considered in

Schedules TCL-2 through 4 due to its immateriality with respect to the overall analysis and impact of this proposed financing.

Q. Please explain Schedule TCL-1, entitled "Actual and Pro Forma Balance Sheet at December 31, 2008."

A. Schedule TCL-1 presents the actual financial position of PEU as of December 31, 2008 and the pro forma financial position reflecting certain adjustments pertaining to the Proposed Financing.

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

A. Schedule TCL-1 reflects the pro forma adjustment to retire the $4.5 million BofA Note with proceeds from the issuance of $6.0 million of CoBank Notes. The $1.5 million difference between the proceeds of the CoBank Notes and the cash used to retire the BofA Note is reflected as an increase in cash (current assets) in the pro forma balance sheet.

Q. Mr. Leonard, please explain Schedule TCL-2 entitled "Actual and Pro Forma Income Statement for the Twelve Months Ended December 31, 2008."

A. As I indicated above, the costs associated with the refinancing are not expected to be significant and are not reflected in Schedule TCL-2. Schedule TCL-2 presents the pro forma impact of this financing on PEU's income statement for the twelve month period ended December 31, 2008.

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

A. Schedule TCL-2 contains two adjustments. Adjustment one is to record the estimated net increase in interest expense related to additional debt raised. I have assumed an interest rate of 6% for the CoBank financing based on discussion with CoBank personnel;

however, the actual interest rate will be based on market conditions at the time of closing. I have also assumed that the additional proceeds will be temporarily invested in short term debt securities at an interest rate of 2.5%. The Company expects that these proceeds will be used to repay intercompany borrowings required to fund capital expenditures in 2009 of approximately $1.2 million and to finance capital expenditures in 2010 of approximately $650,000. The second adjustment is to record the after-tax effect of the additional pro forma interest expense using an effective combined federal and state income tax rate of 39.6%.

Q. Please explain Schedule TCL-3 entitled "Actual and Pro Forma Statement of Capitalization at December 31, 2008."

A. Schedule TCL-3 illustrates PEU's actual total capitalization, as of December 31, 2008, which is comprised of common equity and long term debt including SRF financing.

Q. **Please explain the pro forma adjustments on Schedule TCL-3.**

A. Schedule TCL-3 contains two adjustments. The first pro forma adjustment reflects the after-tax decrease to retained earnings for the additional pro forma interest expense related to the additional debt raised, while the second adjustment reflects the retirement of the BofA debt of $4.5 million and the addition of the $6 million of CoBank debt.

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

A. Yes. PEU's existing agreements contain four covenants governing the issuance of new PEU debt. These covenants specify minimum interest coverage ratios and maximum amounts of debt in relation to net plant and to total capitalization and, lastly, a minimum net worth requirement. While $4.5 million of the $6 million of the proposed CoBank debt simply replaces maturing debt, the net new debt issued is subject to the issuance covenant tests I specified above. PEU's actual ratios, pro formed for the contemplated Cobank Notes , are comfortably within these covenants.

Q. Has PEU's Board of Directors formally voted to authorize the Proposed Financing?

A. Not at this time. Resolutions authorizing the subject financing are scheduled for the next board meeting, which is anticipated to be held on August 5, 2009. Evidence of these resolutions will be provided promptly thereafter.

Q. Do you believe that the Proposed Financing is in the public interest?

A. Yes, I do. The maturity of the BofA Note requires that PEU raise capital to refinance that amount. CoBank, as a government sponsored entity whose mission is to assist vital industries across rural America, offers a low cost of capital source of financing to refinance the maturing debt. In addition, the potential patronage refunds which I expect PEU to receive will further reduce the cost of this capital over the longer term. The additional borrowings being financed will also enable PEU to make appropriate capital improvements as necessary to continue to provide safe, adequate, and reliable water service to PEU's customers and reduce PEU's reliance its parent, Pennichuck, for financing for capital expenditures. The terms of the financing through CoBank are extremely favorable, and lower than the alternative financing options available to PEU to refinance existing debt.

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

A. Yes it does.

Pennichuck East Utility, Inc.
Actual and Pro Forma Balance Sheet as of December 31, 2008
Unaudited
Reflecting the Refinance of $4.5 million BofA Note with $6.0 million CoBank Note

	Actual December 31, 2008	Pro Forma Adjustments		Pro Forma December 31, 2008
Assets				
Plant in Service	$ 29,299,265	$ -		$ 29,299,265
Less: Accumulated Depreciation	(6,690,701)	-		(6,690,701)
Net Plant	22,608,564	-		22,608,564
CWIP	698,088	-		698,088
Total Net Utility Plant	23,306,652	-		23,306,652
Current Assets	829,977	1,500,000	3	2,329,977
Other Assets and Deferred Charges	709,723	-		709,723
Total Assets	$ 24,846,352	$ 1,500,000		$ 26,346,352
Equity and Liabilities				
Common Equity	$ 6,538,021	$ -		$ 6,538,021
BofA Note due 12/31/2009	4,500,000	(4,500,000)	1	-
Current Portion of Long-Term Debt	38,582			$ 38,582
Other Current Liabilities	404,929	-		404,929
Long-Term Bonds	1,469,390	6,000,000	2	7,469,390
LTD--SRF Loans	760,554			$ 760,554
Deferred Income Taxes	2,835,851	-		$ 2,835,851
Contributions in Aid of Construction, Net	8,022,861	-		$ 8,022,861
Other Liabilities and Deferred Credits	276,164	-		276,164
Total Equity and Liabilities	$ 24,846,352	$ 1,500,000		$ 26,346,352

Notes:

1 - To record the retirement of $4.5 million BofA Note.
2 - To record issuance of $6.0 million of CoBank Notes
3 - Net cash proceeds after retirement of BofA Note.

Pennichuck East Utility, Inc.
Actual and Pro Forma Income Statement for the Twelve Months Ended December 31, 2008
Unaudited
Reflecting the Refinance of $4.5 million BofA Note with $6.0 million CoBank Note

	Actual December 31, 2008	Pro Forma Adjustments		Pro Forma December 31, 2008
Operating Revenues	$ 5,088,229	$ -		$ 5,088,229
O&M Expenses	2,985,723	-		2,985,723
Depreciation & Amortization	444,975	-		444,975
Taxes Other Than Income	392,063	-		392,063
Income Taxes	357,669	(20,790)	2	336,879
Total O&M Expenses	4,180,430	(20,790)		4,159,640
Net Operating Income	907,799	20,790		928,589
AFUDC	15,525	-		15,525
Other income (expense), net	-	-		-
Interest Income (Expense):				
Funded Debt	(374,331)	(52,500)	1	(426,831)
Intercompany Debt	(3,782)	-		(3,782)
Total Interest Expense	(378,113)	(52,500)		(430,613)
Net income	$ 545,211	$ (31,710)		$ 513,501

Notes:

1 - To record the change in interest expense associated with refinancing.

2 - To record the tax benefit (39.6%) resulting from additional interest.

Calculation of change in Interest Expense:

Int on $6.0M of CoBank debt	360,000
Less: Int. on BofA debt	(270,000)
Plus: Int. income on additional cash	(37,500)
Net change in interest expense	52,500

Pennichuck East Utility, Inc.
Actual and Pro Forma Statement of Capitalization as of December 31, 2008
Unaudited
Reflecting the Refinance of $4.5 million BofA Note with $6.0 million CoBank Note

	Actual		Pro Forma		Pro Forma	
	December 31, 2008		Adjustments		December 31, 2008	
Common Equity:						
Common Stock	$ 100		$ -		$ 100	
Paid-in Capital	4,000,000		-		4,000,000	
Other Comprehensive Income	(110,875)				(110,875)	
Retained Earnings	2,648,796		(31,710)	1	2,617,086	
Total Common Equity	6,538,021	49.1%	(31,710)		6,506,311	44.0%
Debt:						
BofA Note due 12/31/2009	4,500,000		(4,500,000)	2	-	
Current Portion of Long-Term Debt	38,582				38,582	
Long-Term Bonds	1,469,390		6,000,000	2	7,469,390	
LTD--SRF Loans	760,554				760,554	
Total Debt	6,768,526	50.9%	6,000,000		8,268,526	56.0%
Total Capitalization	$ 13,306,547	100.0%	$ 5,968,290		$ 14,774,837	100.0%

Notes:

1 - To record the annual change in net interest expense, and to record the income tax benefit (39.6%) resulting from additional interest.

2 - To record the retirement of the $4.5 million BofA note and issuance of the $6.0 million CoBank loan.