STATE OF NEW HAMPSHIRE

BEFORE THE

PUBLIC UTILITIES COMMISSION

Re: City of Nashua Acquisition of Pennichuck Corporation

Docket DW 11-026

DIRECT TESTIMONY OF

JOHN L. PATENAUDE

February 18, 2011

Table of Contents

<u>Introduction and Purpose for Testimony</u>

Q. Please state your full name and business address.

A. My name is John L. Patenaude. My business address is 1 Timber Lane, Hudson, New Hampshire.

Q. How are you currently employed?

A. I am currently an advisor to the City of Nashua with respect to the proposed merger transaction with Pennichuck Corporation. My title in this role, pursuant to a contract approved by the City of Nashua Board of Aldermen, is Transaction Executive. The Aldermanic Personnel and Administrative Affairs Committee of the City's Board of Aldermen has recommended my appointment to the office of Interim Chief Executive Officer of Pennichuck Corporation upon completion of the transaction, and the City's Board of Aldermen will consider confirmation of this appointment at its meeting on February 22, 2011.

Q. What is the nature of your work for the City?

A. I have been retained by the City as Transaction Executive to advise it with respect to, and assist in the negotiations and closing of a merger with Pennichuck Corporation. If my appointment as the City's Interim Chief Executive Officer of Pennichuck Corporation is confirmed, I will serve in that capacity upon completion of the transaction.

Q. How long have you been working for the City of Nashua?

A. I have been working as the City's Transaction Executive since June 2010.

Q. Please describe your educational background and work experience.

A. Prior to my current work for the City, I served in various capacities working in financial management positions. Until September 2009, I served as Vice President-Finance, Chief

Financial Officer and Treasurer of Nashua Corporation. Before that position, my other positions with Nashua Corporation included Assistant Treasurer and Director of Taxes. Prior to joining Nashua Corporation in 1991, I worked in various companies, with respect to various financial capacities, including Coopers & Lybrand, Ausimont N.V., Sanders Associates Inc., and John Hancock Mutual Life Insurance Company. I received a B.S. degree in Accounting from Boston College and a M.S. in Taxation from Bentley College. I have been associated with various professional associations, including the Financial Executives Institute (N.E. Chapter); as Director (2001 – 2008) and Chairperson (2006-2007) for the Greater Nashua Chamber of Commerce; and as Director, Gateway Chapter of the American Red Cross (2003-2009).

Q. Have you testified before the New Hampshire Public Utilities Commission or any other utilities regulatory authority on any previous occasions?

A. No.

Q. What are the purposes of your testimony?

A. The purposes of my testimony are: (1) to describe the proposed acquisition of Pennichuck Corporation by the City of Nashua; (2) to provide a summary of the City's and the Mayor's participation in the development and negotiation of terms and conditions of the Merger Agreement between the City of Nashua and Pennichuck Corporation; (3) to explain why this acquisition transaction is structured as a stock purchase rather than a direct purchase of the assets of Pennichuck Corporation or any of its subsidiaries; (4) to describe the proposed financing structure for the acquisition transaction; (5) to discuss the corporate operational structure of Pennichuck Corporation following the merger; (6) to describe the City's plan to implement a "corporate governance approach" to managing

Pennichuck Corporation and its subsidiaries following the merger; and (7) to discuss how this acquisition transaction is consistent with the special legislation that govern this Commission's review of this transaction.

<u>The Merger Agreement and the Proposed Transaction</u>

Q. Are you familiar with the Agreement and Plan of Merger ("Merger Agreement") between the City and Pennichuck Corporation?

A. Yes.

Q. When is the Merger Agreement effective?

A. The Merger Agreement is effective as of November 11, 2010.

Q. What documents comprise the entire Merger Agreement?

A. There is the Merger Agreement itself, and the following attachments to the Merger Agreement:

- Exhibit A: Proposed Articles of Incorporation of the Surviving Corporation;
- Exhibit B: Proposed By-laws of the Surviving Corporation;
- Exhibit C: Settlement Agreement;
- Exhibit D: Confidentiality Agreement; and
- Company Disclosure Schedule.

The Merger Agreement and these attachments are attached to the testimony of Mayor Donnalee Lozeau as Exhibit DL-1.

Q. Please describe the essential terms of the Merger Agreement.

A. Under the Merger Agreement, the City will acquire all of the outstanding shares of Pennichuck Corporation for $29 per share. For this purpose, the City will create a newly-organized subsidiary owned by the City. To accomplish the merger, this newly-organized subsidiary will be merged into Pennichuck Corporation, which will be the surviving corporation. Accordingly, pursuant to the merger, the City will become the sole shareholder of Pennichuck Corporation.

Q. Is the City directly acquiring any shares of any of the corporate subsidiaries of Pennichuck Corporation?

A. No. Pennichuck Corporation will remain the sole shareholder of each of its five subsidiaries, Pennichuck Water Works, Inc. ("PWW"); Pennichuck East Utility, Inc. ("PEU"); Pittsfield Aqueduct Company, Inc. ("PAC"); Pennichuck Water Service Corporation ("PWSC"); and The Southwood Corporation ("TSC"). The corporate ownership structure that results from the completion of the merger is illustrated by the diagram attached as Exhibit JLP-1.

Q. Please describe the consideration to be paid by the City under the Merger Agreement.

A. Section 2.01(c) of the Merger Agreement provides that each share of common stock of Pennichuck Corporation outstanding at the merger date will be converted into the right to receive $29 in cash. The City projects that, at the time of the merger, Pennichuck Corporation will have approximately 4,945,080 shares outstanding and eligible for conversion in the merger. This amount includes stock options that may be exercised to purchase shares eligible for the merger consideration. Accordingly, the total amount of cash consideration to be paid to Pennichuck Corporation shareholders is projected to be approximately $137,793,398.

Q. Please describe the conditions precedent to completing the merger transaction.

A. The conditions precedent to closing the merger transaction are set forth in Article VII of the Merger Agreement. These conditions include: (1) approval by the shareholders of Pennichuck Corporation by a vote of at least two-thirds of the outstanding shares entitled to vote on the merger; (2) approval by the City's Board of Aldermen of the issuance of the bonds necessary to finance the merger by a vote of at least ten members; (3) approval by the City's Board of Aldermen of two fact findings required by the special legislation that authorizes the merger transaction (which is addressed in the testimony of Mayor Donnalee Lozeau); (4) approval by the Commission; and (5) the City's obtaining satisfactory financing terms on which to finance the merger and related costs. While there are other conditions precedent, those that I have listed are the most important ones.

Q. Have any of the conditions you listed occurred as of the date of this testimony?

A. Yes. As indicated in Mayor Lozeau's testimony, on January 11, 2011, the City's Board of Aldermen voted to approve the issuance of the bonds necessary to finance the merger by a vote of 14 to 1. Also, on the same date, the Board voted to make the two fact findings required by the special legislation.

Q. When do the parties anticipate that the Pennichuck Corporation shareholders will vote on the Merger Agreement?

A. The management of Pennichuck Corporation has informed the City that it intends to present the Merger Agreement to a vote of its shareholders at a meeting, which Pennichuck Corporation anticipates will occur in June 2011.

Q. How may the Merger Agreement be terminated?

A. Article VIII of the Merger Agreement sets forth the provisions governing when and how the parties may terminate the Merger Agreement. The parties may terminate the Merger

Agreement by mutual agreement at any time, and a party may terminate the agreement in the event that the other party breaches its representations or covenants. The merger agreement can be terminated if the conditions precedent discussed above are not met. If the merger transaction is not completed by December 31, 2011, then either party may unilaterally terminate the agreement.

Q. Please describe the Settlement Agreement which is attached as Exhibit C to the Merger Agreement.

A. The Settlement Agreement, which was executed by the parties effective as of November 11, 2010, establishes the parties' agreement to settle the eminent domain proceeding docketed by this Commission as DW 04-048. Under the Settlement Agreement, the parties agree that the petition filed by the City in Docket No. DW 04-048 should be dismissed with prejudice upon any termination of the Merger Agreement, at which time the Settlement Agreement requires the filing of a Withdrawal Notice with this Commission.

Reasons For the Stock Acquisition Structure of the Merger Transaction

Q. What are the advantages to the City of the merger transaction, which involves the effective acquisition of the stock of Pennichuck Corporation, compared to an eminent domain taking of the assets of PWW?

A. The City believes that the proposed merger transaction provides a better result than a direct purchase of the assets of any of the Pennichuck companies for three principal reasons.

First, the acquisition of stock of the holding company, Pennichuck Corporation, allows the City to obtain control of important assets that it could not obtain through an eminent domain taking of PWW assets. In Order No. 24,425, issued in Docket No. DW 04-048, the Commission determined that RSA Chapter 38 authorized Nashua to pursue the taking of PWW assets, but not those of PEU or PAC. Accordingly, the focus of the eminent domain proceeding was on the valuation of the PWW assets, and the costs associated with their potential separation from the Pennichuck family of companies. In addition, the eminent domain proceeding did not include the real estate assets owned by another Pennichuck Corporation subsidiary, The Southwood Corporation, which owns land comprising part of the watershed that provide the water supplies that support water service to PWW's customers. This watershed land is viewed as very valuable and important to the City and its citizens. The acquisition of stock of the corporate parent, Pennichuck Corporation, provides an approach that allows the City to acquire the Pennichuck regulated water utilities, the unregulated water service business and the valuable watershed land owned by Southwood.

Second, the acquisition of stock of the holding company can be accomplished at a lower cost than the purchase of the PWW assets alone through eminent domain. In Order No. 24,878 in Docket No. DW 04-048, the Commission determined that the value of the PWW assets as of December 31, 2008, subject to further adjustments to reflect subsequent changes in the net asset base, and excluding a mitigation fund, was $203,031,079. Further, the Commission determined that the City would be required to establish a mitigation fund in the amount of $40,000,000, subject to further proceedings for implementing this result after approving actions by the City's Board of Aldermen. These determinations were approved by the New Hampshire Supreme Court in its opinion issued on March 25, 2010. Accordingly, with these determinations, the City would be required to raise in excess of $243 million (together with updated values through an estimated taking date to be approved by the Commission).

In contrast, under this merger transaction, the total value of the corporations, businesses and assets acquired, along with the outstanding debt assumed, is approximately $198 million (excluding transaction costs), consisting of approximately $138 million to be paid and approximately $60 million in assumed debt. Further, because the City's operating plan, which I discuss in more detail below, provides that all of the Pennichuck corporate entities and businesses will continue to operate as an integrated group of companies with current operating management and employees, there would be no basis for establishing any mitigation fund under this transaction structure. Accordingly, under the proposed merger transaction structure, as compared to the eminent domain scenario, the City will be acquiring more assets at less cost. This comparison is presented in Exhibit JLP-2 attached to this testimony.

Third, the proposed merger transaction permits the City to continue to provide retail water service in the same manner as is currently provided by the Pennichuck utilities, thereby preserving the current operational structure and retaining the jobs of existing Pennichuck employees. During negotiations concerning the Merger Agreement, the parties described this aspect of the proposed transaction and resulting operational structure as "plug and play." What the parties mean by "plug and play" is that, while the City will become the sole shareholder of Pennichuck Corporation in place of the current shareholders, most of the current characteristics of the operational structure of the Pennichuck companies will continue without change. Accordingly, under the proposed "plug and play" approach with its proposed retention of the current Pennichuck corporate and operating structure, the following will stay the same:

- Pennichuck Corporation and its corporate subsidiaries will continue their current existence and legal status as separate legal entities organized and governed under RSA Chapter 293-A as New Hampshire business corporations.
- All of the corporations, including PWW, PEU and PAC, will continue to be operated and managed by the same employees at the operational and customer support level, and from the same locations.
- PWW, PEU and PAC will continue to be regulated by the Commission because they will continue to be "public utilities" within the meaning of RSA 362:2 and 362:4.
- For purposes of ratemaking, the merger will not require a change in the current management and cost allocations among the Pennichuck companies.
- All of the Pennichuck companies, including the three regulated utilities, will continue to pay municipal property and state utility taxes.

Q. What impact does the stock acquisition structure of the proposed merger transaction have on customers of PWW, PEU and PAC?

A. For the reasons described above, including specifically that the City will acquire Pennichuck Corporation and, indirectly, its corporate subsidiaries including the three regulated utilities, for less than the cost of an eminent domain taking of PWW assets by the City, and that the proposed corporate structure will preserve the common operating management synergies currently enjoyed by the Pennichuck companies, the City expects that the rates for each of PWW, PEU and PAC under City ownership will be lower than the level anticipated under current ownership over time. The City's analysis and model supporting this conclusion is presented in more detail in the testimonies of Bonalyn J. Hartley and Arthur Gottlieb.

Q. Are there any other reasons that support the stock acquisition structure of the proposed merger transaction?

A. Yes. The proposed merger transaction and corporate structure will permit a more tax-efficient means of completing the City's acquisition of control over the Pennichuck water operations because it will avoid a triggering of taxable gain and tax liability at the corporate-level either before or after completion of the merger transaction. Pennichuck Corporation and each of its subsidiaries are subject to the federal corporate income tax and report federal income tax as an "affiliated group" within the meaning of section 1563(a) of the Internal Revenue Code. For federal income tax purposes, the merger transaction will be treated as a purchase of Pennichuck Corporation stock directly from its shareholders and so there will be no triggering of corporate-level taxable gain and resultant tax liability, or what is often referred to as "double taxation," that could effectively be charged to the Pennichuck Corporation shareholders in the form of reduced liquidation proceeds. Furthermore, because the City intends to maintain the current corporate structure and does not intend to make any elections that would result in the recognition of taxable gain and tax liability after completion of the merger, the City's acquisition of the Pennichuck Corporation stock pursuant to the merger should also not result in the recognition of taxable gain and tax liability to the Pennichuck companies after the acquisition. If there were to be any such tax liability, this would be addressed by the City as the owner of Pennichuck Corporation. In the present case, non-recognition of gain is especially important because the potential gain amount is substantial. For federal income tax purposes, taxable gain is generally equal to the fair market value of assets treated as sold or exchanged minus their adjusted basis for tax purposes (that is, the original cost of the assets adjusted by items such as depreciation deductions with respect to the assets). The current adjusted basis of many of the assets of the Pennichuck Corporation is significantly lower than the fair market value that is indicated by the purchase price of the proposed merger transaction. The City estimates that the inherent gain, or "built-in gain," could be approximately $105 million, and that the related federal and state corporate income tax cost could be as high as $45 million. The transaction structure being proposed by the parties is designed to avoid this tax liability being triggered since it will result in Pennichuck Corporation and its subsidiaries retaining their current legal status as for-profit business corporations and remaining subject to the federal income tax system following the merger transaction.

Q. Is there any risk that this built-in gain could be recognized as a result of the proposed merger transaction?

A. The City believes that the "built-in gain" should not be recognized for federal income tax purposes because Pennichuck Corporation and its subsidiaries will remain taxable following the merger. If the revenues of Pennichuck Corporation and its subsidiaries were to become excludible from taxation under section 115 of the Internal Revenue Code, there is a possibility that the "built-in gain" would be triggered and the tax liability effectively charged to the City as owner of Pennichuck Corporation. However, the City believes that the proposed structure will allow Pennichuck Corporation and its subsidiaries to continue to operate as a taxable group for federal income tax purposes and, accordingly, the built-in gain should not be recognized for federal income tax purposes.

Financing of the Proposed Merger Transaction

Q. Mr. Patenaude, how does the City propose to finance the costs of the merger transaction?

A. The City plans to raise the funds required to complete the merger transaction through the issuance of general obligation bonds of the City (the "City Acquisition Bonds").

Q. What is the current estimate of the total borrowing to complete the merger transaction?

A. The current estimate of the total borrowing to complete the merger transaction is $157,011,440, exclusive of any borrowing associated with refinancing existing Pennichuck debt, should the City choose to do so at the closing.

Q. Please identify each of the costs that comprise that total amount.

A. The total estimated borrowing is comprised of the following components:

- The consideration to be paid to the shareholders of Pennichuck Corporation pursuant to the Merger Agreement is estimated to be $137,793,398. This amount is based on the current estimate of the number of common shares outstanding or otherwise eligible to receive merger consideration, which is estimated to be approximately 4,945,080.
- Bond issuance costs in the amount of approximately $1,800,000, consisting principally of legal fees for bond counsel and fees for First Southwest, the company the City has retained to provide bond placement advice and services.
- Fees, including legal fees, accounting fees, advisor fees, fees related to due diligence performed by accounting, environmental and engineering firms and investment banker

fees incurred by both the City and Pennichuck Corporation in connection with the negotiation and completion of the merger transaction, which are estimated to be approximately $5,286,875.

- Costs associated with severance packages for certain employees of Pennichuck Corporation management personnel, to be triggered by the completion of the merger and the termination of their employment of $2,131,167.
- The amount necessary to reimburse the City for the costs incurred by the City relating to its efforts to pursue the eminent domain proceeding from January 1, 2002 until August 2009, which is equal to approximately $5,000,000.
- The amount necessary to contribute cash to each of the three regulated utilities to provide a fund that will be used to ensure stable rates in the event of adverse revenue developments (a "rate stabilization fund"), which is $5,000,000 in the aggregate.

The sum of these estimated costs equals the total amount of the estimated costs of completing the merger transaction of $157,011,440. These amounts, and the flow of funds for the merger transaction, are presented in Exhibit JLP-3.

Q. What is the purpose of the rate stabilization fund?

A. The City proposes to establish the rate stabilization fund, to be allocated among the three regulated utilities on a pro rata basis in accordance with their respective rate bases, and contributed to the capital of each of the utilities, as described in more detail in Ms. Hartley's testimony, for the purpose of providing a reserve to ensure that the utilities have sufficient cash, even in adverse conditions such as wet weather, to meet their obligations to permit the City to pay debt service on the City Acquisition Bonds. The proposed amount for the rate stabilization fund was selected because it provided the necessary reserve to address all likely scenarios where utilities might experience an unexpected decline in regular operating revenues. The treatment of the rate stabilization fund for ratemaking purposes is described in more detail in Ms. Hartley's testimony.

Q. Why does the City propose to issue general obligation bonds to finance the merger transaction?

A. The City proposes to issue general obligation bonds to finance the merger for two reasons.

First, using general obligation bonds will allow the City to leave in place Pennichuck's current debt, which is at generally favorable interest rates. If the City were to use revenue bonds to finance the merger transaction, the bonds would be payable solely from revenues from the regulated water utilities and buyers of the bonds would require security arrangements that would trigger an obligation to repay the current Pennichuck debt. In contrast, with general obligation bonds, the bonds are secured by the full faith and credit and general taxing power of the City, and therefore, the buyer does not require the same lien arrangements as in the case of revenue bonds. Accordingly, with general obligation bonds, the City may structure the merger transaction to leave the current favorable Pennichuck indebtedness in place.

Second, based on information obtained by the City from its financial advisors, the interest rate required for general obligation bonds issued by the City would generally be lower than the interest rate required for revenue bonds. Lower interest rates result in lower rates for ratepayers over time.

Q. What are the terms anticipated for the general obligation bonds?

A. The City currently anticipates that it will seek to issue general obligation bonds with the following terms:

- The interest paid on the bonds will be taxable;
- The term of the bonds will be 30 years;
- The bonds may be subject to optional redemption at par by the City at a certain time after issuance; and
- The bonds will be general obligation bonds issued by the City and will not be secured by a pledge of any other assets of the City or the Pennichuck companies.

Q. Why does the City currently anticipate that the interest on the bonds will be taxable, rather than tax-exempt?

A. Under federal income tax law, while a state or political subdivision of a state may generally issue tax exempt bonds, there are limitations when the proceeds of the bonds are used to support "private activity" or to invest in "higher yielding investments." As described earlier, due to other tax concerns, namely avoiding the triggering of a significant federal income tax liability on "built-in gain," the merger transaction is structured to preserve the current corporate and tax status of Pennichuck Corporation and its corporate subsidiaries. This status together with the federal limitations on the use of such bonds is inconsistent with the requirements concerning tax-exempt bonds. Accordingly, the City currently anticipates that interest on the general obligation bonds issued to finance the merger transaction will be taxable under federal income tax laws.

Q. What is the impact of issuing taxable, rather than tax-exempt, bonds?

A. The principal impact is that the interest rate on the taxable bonds will be higher than the interest rate on tax-exempt bonds. Higher borrowing costs results in higher revenue requirements for the three regulated utilities, which means that issuing taxable bonds will be somewhat less favorable for customers than if the City were able to issue tax-exempt bonds.

Q. Has the City considered other strategies that would allow it to issue tax-exempt bonds?

A. Yes. The City has explored alternatives with its advisors, but none of these alternatives have been viable because most of the alternatives would result in the recognition of the "built-in gain" and the significant federal and state income tax liability associated with that gain. As noted earlier, the bonds issued by the City may include a feature that permits the City to redeem them before the end of their term in case the opportunity to refinance the taxable bonds with tax-exempt bonds becomes available.

Q. Has the City determined the feasibility of the general obligation bond issuance it proposes and, if so, at what interest rate?

A. Yes. This question is addressed in more detail in the testimony of John Griffin.

Q. Is there any circumstance relating to financing under which the City would elect not to proceed with the merger transaction?

A. Yes. Under section 7.02(e) of the Merger Agreement, a condition to the City's obligation to complete the merger is that it shall have made financing arrangements that the City reasonably determines are acceptable to the City. This section further provides that this condition will be deemed waived by the City if the City reasonably could have obtained debt financing with certain terms, including that the bonds would have a true interest cost of no greater than 6.50%. Accordingly, if interest rates for taxable general obligation bonds in the capital markets were to increase so that the City could not issue the bonds at a rate at or below 6.50%, the City could elect to terminate the merger agreement and not to proceed forward with the merger transaction.

Q. How did the City determine this 6.50% interest rate condition in the Merger Agreement.

A. This interest rate condition and all of the terms of the Merger Agreement and related agreements were the subject of negotiations between the City and Pennichuck Corporation. As discussed in more detail in Mr. Gottlieb's testimony, based on current financial models prepared for the City, if the interest rate on the bonds were to rise above 6.50%, the viability of the merger transaction would come into question.

Q. How does the City expect to repay the general obligation bonds issued to finance the merger transaction?

A. The City expects that the debt service on the general obligation bonds will be paid from operating income generated by Pennichuck Corporation and its subsidiaries, including the three regulated utilities. As discussed in more detail in Mr. Gottlieb's testimony, the City's financial model indicates that even at the 6.50% interest rate, which may be viewed as the worst case, the operation of the Pennichuck companies at reasonable assumptions should generate sufficient cash flow to service the City's debt service obligations on the bonds with future water rates comparable to those anticipated under current ownership.

<u>Operational Structure of Pennichuck Corporation Following the Merger</u>

Q. How will the City receive the cash from Pennichuck Corporation necessary to pay debt service on the City Acquisition Bonds?

A. As I described earlier, the current corporate structure of Pennichuck Corporation and its subsidiaries will be preserved following the merger. Under the proposed corporate operational structure, the three regulated utilities, and the other current unregulated operations of the other Pennichuck subsidiaries, will continue to operate as they do today, collecting revenues at rates approved by this Commission (with regard to the regulated subsidiaries), and paying operating costs, including debt service on indebtedness that is currently outstanding and also on new indebtedness that will be incurred to finance needed capital improvements. After paying these current operational cash obligations, the subsidiaries will have positive cash flow that they can distribute as intercompany dividends to the parent company, Pennichuck Corporation. Pennichuck Corporation will then use that available cash to pay its obligations to the City in its capacity as sole shareholder.

Q. Has the City determined how Pennichuck Corporation will be capitalized following the merger?

A. The City anticipates that, upon consummation of the merger, it will hold all of the outstanding stock of Pennichuck Corporation as well as a debt obligation from Pennichuck. The City anticipates that Pennichuck Corporation will be capitalized at an equity to capitalization ratio of 20%. This capital structure will allow Pennichuck Corporation to pay cash to the City in the form of dividends on stock and as principal and interest payments on debt.

Q. Does this corporate operating structure have implications for ratemaking for the three regulated utilities?

A. Yes. As noted in Mayor Lozeau's testimony, it is fundamental for the City that the level of rates for each of the regulated utilities must be sufficient to generate the cash required to permit the City to pay debt service on the City's Acquisition Bonds. As described in more detail in Ms. Hartley's and Mr. Gottlieb's testimonies, the City is requesting that the Commission leave in effect current rates for each of the Pennichuck utilities subject to the determinations in rates currently under consideration for PWW and PAC in Docket Nos. DW 10-090 and DW 10-091, and approve a method for the establishment of rates for the Pennichuck utilities in the future that provides the Pennichuck utilities with the ability to obtain sufficient revenues to service their portion of the debt required to consummate the proposed transaction.

<u>Governance Structure for Pennichuck Corporation and its Corporate Subsidiaries</u>

Q. What is the City's plan for the governance of Pennichuck Corporation and its subsidiaries following completion of the merger transaction?

A. The City plans to establish a corporate governance system for purposes of managing its ownership of Pennichuck Corporation. This corporate governance system would be very similar to the one that currently governs the company and its subsidiaries, with the exception that the City would be the sole shareholder, replacing the hundreds of shareholders that currently own shares in Pennichuck Corporation. Upon completion of the merger, the articles of incorporation and by-laws of Pennichuck Corporation will be in substantially the form attached to the Merger Agreement as Exhibit A and Exhibit B, respectively. Under these documents, the management of the business and affairs of Pennichuck Corporation will be vested in the board of directors. The board of directors will annually elect officers to manage the day-to-day operations of Pennichuck Corporation and its subsidiaries.

Q. How will the Pennichuck Corporation board of directors be constituted?

A. The board of directors will be comprised of between 7 and 13 members, including both residents of the City and residents of the other communities served by PWW, PEU and PAC. At least five of the members must be residents of Nashua, at least one member must be a user of the water system from outside of Nashua and, for the first two years after completion of the merger transaction, one must be the Mayor of Nashua.

Q. How will the members of the Pennichuck Corporation board of directors be selected?

A. The membership of the first board will be designated in the by-laws established by the City before the completion of the merger. Following that first board, new directors will be nominated and elected in accordance with the process set forth in the by-laws. Under that process, candidates for the board must be nominated by the board and then submitted for election by the City, in its capacity as sole shareholder, at the annual meeting of the corporation.

Q. Has the City identified the members of the first board?

A. The City is in the process of recruiting and interviewing board members, but has not made any selections at this time. The City anticipates seeking broad representation of the various constituencies that have interests in the operations of Pennichuck and its subsidiaries, including to the extent possible representation from customers of PAC and PEU.

Q. Are there any restrictions on who may serve as a member of the Pennichuck Corporation board of directors?

A. Yes. Under the by-laws, except for the Mayor of the City who is to serve for the first two years following the merger, elected officials, key public employees and their family members may not serve on the board. This restriction was carefully crafted by the City's Mayor and Board of Aldermen in order to minimize the influence of elected officials or public employees on the operations of Pennichuck Corporation and its corporate subsidiaries.

Q. How will the City exercise its authority as the sole shareholder of Pennichuck Corporation?

A. All decisions that must be made by the shareholder will be made by the City acting by vote of the Board of Aldermen, subject to veto of the Mayor. This decision-making process is the same process used by the City for regular business.

Q. Has the City determined who will serve as officers of Pennichuck Corporation following the merger?

A. Pennichuck's senior management team currently consists of a Chief Executive Officer, a Chief Financial Officer, a General Counsel, a President of the three regulated utilities, a President of the Water Service Company and a Vice President of Administration and Regulatory Affairs. After the completion of the acquisition, the City expects that the current CEO will be replaced, and that the current position of General Counsel will be eliminated. In addition, the current Controller will become the new Chief Financial Officer, eliminating another position. These officer-level positions, which will be replaced or eliminated, are currently held by executives whose backgrounds and duties have related directly to Pennichuck Corporation's status as a publicly-traded company. Upon completion of the merger, the company will no longer be publicly-traded, so these changes will be appropriate. The City expects that the position of President of Regulated Utilities will be elevated to the Chief Operating Officer of the Pennichuck Corporation and its subsidiaries, with operating responsibility for both regulated and non-regulated companies. This position will be filled by Donald Ware. The position of President of the Water Service Company and the responsibility for the operations of the Water Service Company will be consolidated under the Chief Operating Officer, thereby eliminating one additional position and reducing administrative cost. The position of Vice President of Administration and Regulatory Affairs will be retained. PWW's operating management below the executive officers, and remaining staff, are not expected to change materially as a result of the acquisition. It is anticipated that the operating staff under the leadership of the Chief Operating Officer will continue to provide the same quality service to existing customers of the three regulated utilities from the same locations.

Q. Does the City intend to establish a Chief Executive Officer position?

A. Yes. The City intends to appoint an interim Chief Executive Officer ("CEO") to lead the Pennichuck Corporation management team during a transition period to be defined by the Company's Board of Directors. As I noted earlier, the Aldermanic Personnel and Administrative Affairs Committee of the City's Board of Aldermen has recommended my appointment to the office of Interim Chief Executive Officer of Pennichuck Corporation upon completion of the transaction, and the City's Board of Aldermen will consider confirmation of this appointment at its meeting on February 22, 2011.

The interim CEO will report to the Pennichuck Board of Directors. The primary duties of the interim CEO will be as follows:

- ensure continuity of service to customers;
- transition the Company from a publicly-traded company to a municipally-owned company;
- maintain the Company's financial stability in order to insure the servicing of the debt issued to acquire the Company and the funding of capital required in the business;
- lead the Company through the transition of the management team as certain members of the current team depart and other members of the management team take on additional management responsibilities;
- work with the management team to revise budgets, establish short and long term strategies including capital improvement plans for the regulated and non regulated businesses;
- institute succession planning in order to insure the availability of management talent for the future;
- work with the Board of Directors and management team relative to the fiduciary responsibilities related to the company's pension plans;
- at the direction of the Board of Directors, communicate with the City in its capacity as sole shareholder of the company; and
- perform other duties and tasks as may be assigned by the company's Board of Directors.

Q. What impact will the City's proposed reorganization of corporate management have on the operating costs of Pennichuck and its corporate subsidiaries?

A. The proposed reorganization of corporate management set forth above will significantly lower such operating costs. As set forth in Exhibit JLP-4, this reorganization in corporate management will reduce the annual operating costs of Pennichuck Corporation by an estimated $586,203; and will reduce the annual operating costs of PWW by an estimated $1,156,203, for a total estimated annual savings of $1,742,406.

Q. Do you have any further testimony at this time?

A. No.