STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES PUC

Re: City of Nashua Acquisition of Pennichuck Corporation and Taking of Pennichuck Water Works, Inc.

Docket No. DW 11-026

<u>TESTIMONY OF FINLAY C. ROTHHAUS</u>

Q: Please state your name and public office.

A: My name is Finlay C. Rothhaus and I am Chair of the Merrimack Town Council which serves as the governing body of the Town of Merrimack ("Merrimack").

Q: Please summarize your testimony.

A: This testimony expresses the Merrimack's concern with the proposed merger acquisition of the Pennichuck Corp. by the City of Nashua as proposed in this Docket. Merrimack is concerned that this acquisition may not be in the public good. However, if certain conditions are met, Merrimack's opposition may be mitigated. The concerns are generally in five areas.

There is an issue corporate governance of the resulting city owned utility, where ratepayers are not allowed representation on the Board by right, but only at Nashua's discretion. A second issue is that Merrimack ratepayers share inordinately in the risks of owning a utility, especially one whose acquisition costs and capital expenditures are funded completely by debt. A third concern is that Nashua's control of the utility may result in discrimination against Merrimack in terms of allocation of resources, due to Merrimack having a substantial commercial/industrial district served by the core Nashua system. A fourth concern is that the issue of regionalization has not been adequately considered, due to Nashua's reluctance to adopt any regional approach to public utility water service. Last, Merrimack is concerned that the request by Nashua for the ratepayers to fund transaction and litigation costs in the amount of 12.4 Million and the revenue stabilization in the amount of $5 Million is unfair to ratepayers outside of the City of Nashua's borders.

Q: What concerns do you have about corporate governance in the event the acquisition as proposed is stated?

A: The By-Laws of the merged corporation, which is proposed to be wholly owned by Nashua, provide for governance by a 15 person Board of Directors. Unlike publicly held corporations, there is no effective check on this governance in the form of an annual meeting or special meetings of the ratepayers. All shares are owned by the City of Nashua. Therefore, any role by the ratepayers as a whole is not contemplated. Rather the Directors have almost unfettered discretion, except with regard to certain defined limitations where Nashua's Board of Alderman can intervene. One of these limitations is that the Alderman have final say regarding capital expenditures. See Amended and Restated Articles of Incorporation, Article IX, Section 3.[1] This effectively makes that capital expenditure decision a political process. Non-Nashua ratepayers will have to bear the cost of these debt-funded capital expenditures, without any assurance they will be dealt with fairly in that political process. Additionally, Nashua appoints all Directors. None of the other ratepayer communities[2] have any role in the selection of Directors, nor can they claim the Board seat as a matter of right. Although Nashua has committed to seeking nominations from other ratepayer communities, it is under no obligation to select any of the nominees so nominated. In fact, it appears to have rejected a qualified individual proposed as a candidate by Merrimack.

[1] It is unclear to me whether the Merger Agreement and proposed Articles of Incorporation are subject to a Confidentiality Agreement. Therefore, I refer you to Exhibit A of the Merger Agreement, amended and Restated Articles of Incorporation attached to Mayor Lozeau's pre-filed testimony.
[2] The term "ratepayer communities" refers to those in the Town of Merrimack, PAC and PEU customers.

At the very least Merrimack requests that one or more Board seats be allocated to persons nominated by Merrimack.[3] Consideration should also be given to nominees by right from the other ratepayer communities of PAC and PEU.

Q: Please describe your concerns about risk sharing.

A: I believe the testimony filed by Scott Rubin for the Office of the Consumer Advocate and Mark Naylor for the PUC Staff addressed these issues better than I can. However, Merrimack has been concerned throughout these proceedings that the acquisition costs, capital expenditures and presumably operating deficits would be funded completely by debt. This assumes that Nashua will have access to the debt markets at reasonable rates indefinitely into the future. It also increases the risk that without some mechanism for equity infusions, capital requirements and operating deficits could be directly passed onto the ratepayers on a cash flow basis, something that could result in rate shock. It is unclear to Merrimack whether the PUC regulatory oversight would be sufficient in this case to anticipate and prevent such a rate shock. At least the recommendation of Mr. Rubin and some of the recommendations of Mr. Naylor address this issue in terms of forward-looking rate making mechanisms. Merrimack endorses the distinction advanced by Mr. Rubin, and reflected in Mr. Naylor's testimony, between owner-customers and non-owner customers. Rate setting methodology that recognizes that distinction is more equitable to non-owner customers, in that they will not be asked to share costs and risks of ownership while sharing none of its benefits. Also, as discussed below, Merrimack does not feel that there is any reason why it should share in the expenses incurred by Nashua in pursuing the eminent domain proceeding of $5 Million, severance costs in the amount of $2.1 Million and

[3] Merrimack has a distinct interest from PAC and PEU ratepayers, since it is part of the Nashua core system and, according to data responses filed by the Joint Petitioners, represents 4.8% of the PWW's revenue and 10.1% of the PWW's consumption (Attachment 1).

transaction costs of $5.3 Million. Nor does Merrimack understand why it and other extra-territorial ratepayer communities should fund the $5 Million rate stabilization fund, as both the OCA and PUC Staff also questioned. These are expenses and risks of ownership not contributory to the operation of the utility.

Q: Based on the above testimony, do you have any recommendation?

A: If the PUC were to approve this transaction, Merrimack adopts the recommendations of Mr. Rubin for conditions to be incorporated into the approval and enforceable by the PUC.[4] This would mitigate the risk sharing problem through the creation of distinct rate setting districts so that certain costs and benefits are allocated to the City of Nashua ratepayers, as owners. Also, Mr. Rubin's recommendations would provide for a forward-looking rate making structure that recognizes the distinction between owners-customers and non-owners customers. To the extent that they are consistent with Mr. Rubin's recommendations, Merrimack also adopts the recommendations of Mr. Naylor. On Page 15, Line 18 of Mr. Naylor's testimony, however, Mr. Naylor may have ignored that Merrimack is a separate customer class in terms of his recommended cost of service study; and the PUC should consider this possible omission when it adopts the conditions. To the extent that Mr. Naylor has recommended conditions which do not fully reflect the rate setting mechanism recommended by Mr. Rubin, we recommend the adoption of Mr. Rubin's recommendations as conditions of approval.[5]

Q: What is your concern about Nashua discriminating against Merrimack in terms of allocation of resources?

A: Merrimack's still developing, southern industrial/commercial zone borders Nashua's Route 101-A commercial corridor. If Merrimack is not represented on Pennichuck's Board, the

[4]. Mr. Rubin's recommendations are found on Pages 29-31 of Mr. Rubin's direct testimony and are not reproduced here.

[5] Mr. Naylor's recommendations are contained on Page 16 of his direct testimony and are not reproduced here.

allocation of resources, including capital expenditures, is entirely within Nashua's discretion. While this may be mitigated somewhat, if PWW is a regulated subsidiary, its parent corporation is owned by the City of Nashua and is itself unregulated. These are problems that Merrimack does not encounter at present because the Pennichuck Corporation has always been a regional-minded and responsive public utility, whose interest in responsible expansion have been encouraged by the PUC. In this regard, Merrimack also has a water district serving its central portion. Pennichuck supplies the emergency connection to that water district's water system. That water district in turn wheels Pennichuck water through the customers of Amherst and Bedford. Anheuser-Busch is its largest employer and a Pennichuck customer and receives its water by special contract. Mr. Rubin's testimony addressed the ambiguities of Nashua's position as to Anheuser-Busch at Pages 22-23.

Therefore, the previously expressed issues of risk sharing and corporate governance must be addressed in order to recognize Merrimack's unique position as a ratepayer and non-owner community.

Q: You also expressed a concern about regionalization. Could you address this?

A: Merrimack has always been concerned about the regionalization issue. In this respect, its interest extend beyond the Merrimack ratepayer community, in that it has generally been Merrimack's understanding that regionalization was in the public interest because water resources are dwindling. This is a question of vision, but this docket presents an opportunity for the PUC to address the regionalization issue. Nashua has expressed that it will only expand into communities that Pennichuck already services.[6] However, the history of Pennichuck as a regulated utility is that it has been as a first resort for distressed municipal and private water systems. If the Nashua owned utility will resist expansion, there is no such first resort. While

[6] See Response to Staff Data Request 1-32(b), attached as Attachment 2.

Merrimack has no specific recommendation in this regard, it believes that this is an issue the PUC should consider, both in determining whether this transaction is in the public's good, but also in terms of the conditions it imposes if it does find the public good served.

Q: Merrimack also expressed a concern about funding certain costs associated with the acquisition and the revenue stabilization fund, have you addressed this in previous questions and answers?

A: I addressed this in my answer on Pages 3 and 4 of my direct testimony. These concerns would be addressed if the conditions to PUC approval of this acquisition suggested by Mr. Rubin, and those of Mr. Naylor that are consistent with it, were adopted by the PUC as part of its approval.

Q: Does this conclude your testimony?

A: Yes it does.

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Finlay C. Rothhaus

STATE OF NEW HAMPSHIRE
COUNTY OF HILLSBOROUGH

Before me appeared the above-named Finlay C. Rothhaus and made oath that the above statements are true to the best of his knowledge and belief.

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Notary Public/Justice of the Peace
My Commission Expires: