STATE OF NEW HAMPSHIRE

BEFORE THE

PUBLIC UTILITIES COMMISSION

Docket No. DW 17-128

Pennichuck East Utility, Inc.
Request for Change in Rates

DIRECT TESTIMONY OF LARRY D. GOODHUE

September 26, 2017

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I. INTRODUCTION

Q. Would you please state your name, address and position with Pennichuck East Utility, Inc.?

A. My name is Larry D. Goodhue. My business address is 25 Manchester Street, Merrimack, New Hampshire. I am the Chief Executive Officer and Chief Financial Officer of Pennichuck East Utility, Inc. (the "Company" or "PEU"). I have been employed with the Company since December, 2006. I am also the Chief Executive Officer, Chief Financial Officer and Treasurer of Pennichuck Corporation ("Pennichuck"), which is the corporate parent of PEU.

Q. Please describe your educational background.

A. I have a Bachelor in Science degree in Business Administration with a major in Accounting from Merrimack College in North Andover, Massachusetts. I am a licensed Certified Public Accountant in New Hampshire; my license is currently in an inactive status.

Q. Please describe your professional background.

A. Prior to joining Pennichuck, I was the Vice President of Finance and Administration and previously the Controller with METRObility Optical Systems, Inc. from September, 2000 to June 2006. In my more recent role with METRObility, I was responsible for all financial, accounting, treasury and administration functions for a manufacturer of optical networking hardware and software. Prior to joining METRObility, I held various senior management and accounting positions with several private and publicly-traded companies.

Q. What are your responsibilities as Chief Executive Officer of Pennichuck Corporation?

A. As Chief Executive Officer, I am responsible for the overall management of Pennichuck and its subsidiaries, including PEU, and I report to the Board of Directors. I work with the Chief Operating Officer, the Corporate Controller, Assistant Treasurer, the Director of Human Resources and the Director of Information Technology to: (1) implement short and long-term financial and operating strategies, (2) insure the adequate funding of debt and expenses, and (3) enable Pennichuck's utility subsidiaries to provide high quality water service at affordable rates, on a consistent basis.

Q. Have you previously testified before this or any other regulatory commission or governmental authority?

A. Yes. I have submitted written testimony in the following dockets before the New Hampshire Public Utilities Commission (the "Commission"):

- Financings for PEU – DW 12-349, DW 13-017, DW 13-125, DW 14-020, DW 14-191, DW 14-282, DW 14-321, DW 15-044, DW 16-234 and DW 17-055;
- Financings for Pittsfield Aqueduct Company ("PAC") – DW 15-045 and DW 16-235;
- Financings for Pennichuck Water Works, Inc. ("PWW") – DW 14-021, DW 14-130, DW 15-046, DW 15-196, and DW 16-236.
- Permanent and Temporary Rate Increase Proceedings for: PWW – DW 13-130 and DW 16-806; PEU – DW 13-126; and PAC – DW 13-128.

II. PURPOSE OF THIS TESTIMONY

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to provide information supporting PEU's request for temporary and permanent rate relief, including: (1) relevant historical information regarding the City of Nashua's acquisition of Pennichuck in early 2012; (2) information concerning how the ratemaking structure set forth in the Settlement Agreement approved by this Commission in Order No. 25,292 in Docket No. DW 11-026 has been operating since the 2012 acquisition; (3) information concerning PWW recent settlement modifying its ratemaking structure in Docket No. DW 16-806 should be applied to PEU; and (4) information supporting the rate relief requested by PEU and the specific modifications to PEU's current ratemaking structure demonstrating that such requests are just, reasonable and in the public interest. I note that, while PEU is applying the modified rate methodology that is described in PWW's Settlement Agreement filed in DW 16-806, as of the filing of PEU's rate case, the Commission has not yet issued a ruling on that Settlement. If the Commission modifies the Settlement in its order, PEU will supplement its filing as may be necessary under the Commission's order.

Q. Would you please identify the other witnesses in this case?

A. The other witnesses in this case, both of whom are providing written testimony in this proceeding, are Chief Operating Officer Donald Ware and Chief Engineer John Boisvert. Both of these individuals hold these roles for both PEU and Pennichuck, as well as the other subsidiaries of Pennichuck. Their testimonies will describe their qualifications, history and previous instances of testimony before the Commission.

III. HISTORY OF THE CITY OF NASHUA ACQUISITION

Q. Mr. Goodhue, before explaining the details of the proposed financings, would you please provide some history regarding the ownership of PEU and how that history supports PEU's request for approval of permanent and temporary rate relief?

A. PEU as a corporate entity is wholly-owned by Pennichuck, which is, in turn, a closely-held private corporation that is wholly-owned by the City of Nashua, New Hampshire. The City of Nashua acquired its ownership of Pennichuck on January 25, 2012, pursuant to this Commission's Order No. 25,292 (November 23, 2011) (Approving Acquisition and Settlement Agreement). Prior to this acquisition by the City of Nashua, Pennichuck's shares were traded on the NASDAQ public stock exchange. For purposes of my testimony, I refer to the period prior to the City's acquisition as "pre-acquisition" and the period after as "post-acquisition."

Q. Did the City's acquisition affect the way in which PEU operates as a utility?

A. Yes. The change in the ultimate ownership of PEU's parent, Pennichuck, from a publicly-traded investor-owned utility to ownership by the City has had important consequences for the operation of PEU. These same issues were involved with PEU's sister company, PWW which is also wholly owned by Pennichuck. As such, my testimony in PWW's recent rate case, Docket No. DW 16-806, applies equally to this case. In light of the recent settlement regarding PWW's ratemaking methodology, I will be referring to PWW's recent rate case in DW 16-806 throughout my testimony.

Q. What are the important similarities in the way the City's acquisition affected the operation of PEU and PWW?

A. One of the most important consequences is that both PEU and PWW, after the City's acquisition of Pennichuck, no longer have access to the private equity markets as a method of financing a portion of their capital needs, like most Investor Owned Utilities ("IOU's"), whereby a 50/50 debt/equity ratio is considered optimal, but at an elevated cost to rate payers due to a return on equity needed to benefit public company shareholders. As such, and as contemplated during the Commission's proceeding to approve the City's acquisition of Pennichuck in DW 11-026, after the acquisition, PEU and PWW are expected to finance their on-going capital needs entirely through the issuance of debt.

Q. Does reliance solely on debt to finance PEU's operations have impacts on PEU's customers?

A. Yes. As contemplated during the acquisition proceedings, one positive result of this anticipated debt financing is that the weighted cost of PEU's capital structure is significantly lower than it was prior to the City's acquisition, due to the elimination of the public company ROE dynamic discussed previously, as for PEU this ROE existed at 9.75% post-tax pre-acquisition (approximately 16% pre-tax). This lower cost of capital has had and will continue to have direct beneficial benefits for PEU's customers.

Q. Does reliance solely on debt to finance PEU's operations have consequences for PEU's rate setting methods and procedures?

A. Yes. As also contemplated in the acquisition Docket DW 11-026, the City's acquisition of Pennichuck and the resulting need to finance utility operations solely with debt has required modifications to PEU's (and Pennichuck's other utilities') ratemaking methods and procedures. As a result of this reliance on debt, PEU is much more dependent on the direct relationship of cash flow generated from rates, as it relates to the ongoing repayment of debt in support of ongoing capital investments. Under the previous ownership structure, the allowed return on public company equity allowed for extra cash generated to cover the repayment of debt obligations, as well as adequate coverage of operating expenses and dividend obligations to shareholders.

IV. RATEMAKING METHODOLOGY SETTLEMENT IN PWW'S RATE CASE, DOCKET NO. DW 16-806

Q. Mr. Goodhue, you noted the impacts of the City's acquisition of Pennichuck on its subsidiaries, including PEU and PWW, were similar. Please provide an overview of PWW's 2016 rate case.

A. In PWW's Docket DW 16-806, we were faced with many of the same issues that presently face PEU. The City's acquisition resolved almost a decade of intense disputes between the City and the pre-acquisition management of Pennichuck, and was premised on the assumption that the City's ownership of the utilities would produce consistently lower rates for ratepayers over time, as compared to the previous investor-owned utility structure. On July 19, 2017, the Parties to Docket DW 16-806 filed a Settlement Agreement which substantively updated the ratemaking methodology adopted in Docket DW 11-026. As is outlined in the DW 16-806 Settlement Agreement, Pennichuck's experiences since the DW 11-026 ratemaking methodology was approved demonstrated some deficiencies in that methodology, but our experience also provided a basis to understand what improvements to the methodology were needed. Those improvements are reflected in the DW 16-806 Settlement. The DW 16-806 Settlement Agreement is attached as Exhibit LDG-1 (excluding exhibits).

Q. What are the primary benefits of the DW 16-806 Settlement Agreement?

A. The modifications to PEU's ratemaking structure will increase PEU's required access to the credit markets, provide adequate cash flows to repay their debts, give them the ability to meet lender covenant requirements, and will provide lenders with the confidence in PEU's ability to repay their debt obligations, all of which is fundamental for PEU to be able to continue to access needed debt for infrastructure replacement and operations.

Q. Did the Parties to the DW 16-806 Settlement Agreement anticipate that the modified rate structure would also apply to PEU?

A. Yes. The Settlement Agreement specifically includes the following provision on pages 14-15: "*The Settling Parties agree that the current $5,000,000 Rate Stabilization Fund (RSF) maintained by PWW, which was established under the Original Rate Structure, should be re-allocated amongst the three Penn Corp utilities such that PWW's allocated share of the RSF shall now be $3,920,000, with the remaining balance of $1,080,000 to be allocated between PEU and PAC. The allocation to PWW is based on the respective three utilities' last Commission approved revenue requirements as detailed on Exhibit 6 of this Settlement Agreement. The Settling Parties agree that the $1,080,000 portion of the RSF that is proposed to be allocated between PEU and PAC shall remain in PWW's RSF cash account until such time that rate case filings are made for PEU and PAC. At that time, the modified rate structure for PWW that is proposed in this settlement agreement will also be requested as the proposed rate structures for both PEU and PAC.*

If the respective rate structures for PEU and PAC are approved by the Commission, the $1,080,000 will then be transferred from PWW's RSF funds to the respective RSF funds to be established in PEU and PAC."

Q. Is PEU now seeking to implement the same ratemaking structure described in the 16-806 Settlement Agreement?

A. Yes. This is the ideal time for the new ratemaking structure to apply to PEU. PEU currently has lender covenants in place that exceed its ability to meet those requirements, and fully cover its cash flow obligations and covenant compliancy, under its existing rate structure, given the fact that PEU's depreciation lives are well in excess of its debt instrument lives, giving rise to the fact that the cash flow generated from depreciation does not fully meet the principal repayments on issued debt. Additionally, as PEU has no current access to the RSF funds at PWW, with the ability to repay any monies borrowed from those funds, the new methodology is needed to: (1) insure adequate EBITDA coverage for PEU, as it relates to covenant requirements, (2) provide adequate cash flows from revenues to pay debt service, CBFRR and operating expenses, and (3) provide adequate support funds in the form of the RSF accounts, to provide for cash funding during times of revenue shortfalls and expense growth above inflationary levels between rate case filings.

Q. Of the $1,080,000 of RSF funds to be transferred from PWW to PEU and PAC, how much is reserved for PEU, and if that amount is insufficient to fully fund those RSF accounts, how does the Company anticipate handling the full funding of those accounts?

A. Of the $1,080,000 in RSF funds available from transfer from PWW to PEU and PAC, $980,000 is reserved for PEU and $100,000 for PAC. As delineated in Mr. Ware's testimony in support of this filing, the calculated need to fully fund the new RSF accounts is actually $1,330,000. As such, the available transferrable cash funds are $350,000 short of the overall assessed need at this time. This shortfall is anticipated to be funded in one of the following ways: (1) to the extent the Company is able to collect refunds from its property tax abatement and litigation proceedings, for previous years taxes returned to the Company, it will seek approval internally from its Board of Directors to allocate those funds as additional funding to establish the RSF accounts, (2) to the extent that the Company monetized certain real property assets currently being pursued as available for sale, as they are no longer used for well sites, booster station sites, or other water supply purposes, the Company will seek approval internally from its Board of Directors to allocate those funds as additional funding to establish the RSF accounts, and (3) to the extent that the funds are still inadequately funded, the Company will seek full funding of those accounts in its next promulgated future rate case.

Q. Are there any differences from the Settlement Agreement that PEU is asking for at this time?

A. Yes. There is one exception to how we are asking to implement the modified rate methodology. We propose to phase in the five-year test year revenue averaging into two phases; implementing 50% of the impact of that change with this rate case, and then fully implementing it with PEU's next rate case.

Q. Before we discuss why PEU is asking for this phased-in approach, please describe how the five-year averaging works under the modified rate methodology.

A. The purpose of the five-year averaging is to develop pro forma test year data regarding revenues and expenses which is less likely to reflect unusual or abnormal events, such as a uniquely dry or wet summer. Under the DW 16-806 modified rate methodology, the "test year" revenues use the trailing five-year average consumption at the most recently approved volumetric rates and fixed charges. The five-year trailing average consumption determination shall be based on the four calendar years immediately preceding the designated test year for which the rate case is filed as well as the test year itself. Additionally, all direct test year expenses which are affected by differences in consumption, including but not limited to purchased water expense, electricity expense, and chemical treatment expense, also include pro forma adjustments to reflect the pro forma difference in consumption between the five-year average and the test year. Although the modified methodology includes this five-year average test period for computing its revenue deficiency, the Settlement Agreement specifically states that neither Staff nor the OCA are precluded from making an alternative recommendation in place of the five-year average with respect to the determination of revenue deficiency.

Q. Please describe how you are asking the five-year average be implemented for PEU.

A. As I noted earlier, we are proposing to phase in the five-year averaging over two rate cases. We plan to calculate the full effect of the five-year average for the 2016 test year under this rate case, and include 50% of the impact of that pro forma calculation into this filing. At our next rate case, we will compute the five-year average for that test year, and include 100% of its impact in that next filing. Even though the Company desires to get onto the five-year average method as soon as possible, the impact on customers to phase it in 100% in this rate case represented approximately an additional 2.5% increase in current rates. As we felt this to be overly onerous, we have elected this two-phase approach, with the understanding that this would represent nearly $180,000 in reduced revenue request in this filing. Part of the rationale in being able to take this approach results from the cash generated from revenues in 2016, due to elevated consumption levels from the drought conditions. Additionally, we offer this approach with the understanding that it may cause the Company to utilize the RSF funds established in this case, at a little greater level between this rate case and the next filed rate case, should revenue levels dip significantly in the years between cases.

V. OVERVIEW OF REQUESTS FOR RATE RELIEF AND MODIFICATIONS TO PEU'S RATEMAKING STRUCTURE

Q. Mr. Goodhue, before describing the details of the proposed request for permanent rate relief, could you provide an overview of the nature of the proposal?

A. The proposed rate relief proposal consists of two principal components. First, as set forth in our full rate filing materials which are described in more detail by Mr. Ware in his testimony, PEU is requesting an increase in annual revenues of approximately $1,399,075, or 20.35%. Second, to account for asset additions made in 2017, PEU will be seeking a step increase of approximately $79,017, or 1.15%. The requested increases will result in a total increase of approximately 21.50%. The third component of PEU's requested relief is its request, as I described above and as is set forth in PEU's Petition for Further Modifications in Ratemaking Structure, for approval of the modified ratemaking methodology as was applied to PWW in Docket No. DW 16-806. Adopting the DW 16-806 modified ratemaking methodology would allow PEU to provide adequate cash flow to cover its overall cost of operations, including prudent operating expenses and debt service costs, and provide its debt lenders with reasonable expectations of future rates that are directly related in a common sense way to PEU's long-term, post-acquisition capital requirements which rely on almost entirely on debt. To restate this, essentially these modifications expressly acknowledge that PEU's reliance on debt financing requires a ratemaking method that is based on a fixed multiple of the annual debt service on existing debt, with the balance of the allowed revenue requirement tied to coverage of prudent, normal and ongoing operating expenses.

Q. In this request for rate increases, are there specific requests that PEU is making to reduce the overall increase in rates to its consumers?

A. Yes. We worked very hard to reduce the overall impact of this rate case on PEU's consumers. In addition to implementing the DW 16-806 methodology which should have long-term beneficial impacts, we are asking the Commission to eliminate the 4 ccf minimum applicable only to PEU's North Country systems (Birch Hill in North Conway, Sunrise Lake Estates in Middleton and Locke Lake Colony in Barnstead). In Docket Nos. DW 08-052 and DW 09-051 (consolidated by Order No. 24,975 (June 5, 2009)), the North Country systems were transferred from PAC to PEU. The 4 ccf minimum was applied based on the lower than average usage in the North Country systems due to the high percentage of seasonal residents, for those systems in the aggregate, at that time. As a result, PEU would not have been able to collect revenues sufficient to cover operating expenses, absent the 4 ccf minimum monthly billed amounts. *See* Order No. 24,975 at p. 18-19. Since the 2009 Order, however, the ratio of seasonal and year-round residents has shifted considerably, such that PEU now believes it can cover operating expenses based on actual usage without applying a 4 ccf minimum. Although PEU will likely experience a short term loss in revenue, we believe those losses can be absorbed. Additionally, eliminating the 4 ccf minimum has two additional impacts that are important to observe: (1) a good portion of the residents in those systems that were seasonal residents in the past, are now full year retired residents using far less than 4 ccf per month for actual consumptive purposes, and (2) the Company has had to implement certain outside watering restrictions for the residents in the Locke Lake system on a recurring annual basis (and for residents in all three systems in the fall of 2016), due to supply concerns which were exacerbated during the extended drought from mid-2015 through early 2017. As such, the 4 ccf minimum is contrary to normal use levels for full year residents in those systems, as they are now comprised, and it is also at odds with the water conservation and stewardship measures that the Company regularly maintains for those systems.

Q. What other requests is PEU making in this rate case to reduce the overall increase in rates to its consumers?

A. In the same 2009 Order No. 24,975, the Commission approved a capital recovery surcharge to recover all capital costs, including the purchase price, for the North Country systems. The surcharge was based on system-specific capital improvement costs and was to be recovered over thirty-years. PEU plans to reduce the surcharge that currently applies to Birch Hill and Locke Lake by refinancing existing inter-company loans, which are directly tied to these surcharges, whereby the terms of those loans will be extended at current estimated cost of borrowed fund rates. This revised surcharge will not apply to Sunrise Lake Estates, as it would cause the surcharge on those customers to increase, contrary to the overall intent in this action. PEU is unable to achieve a complete elimination of the surcharge at this time because of the resulting negative impact it would have on PEU's other consumers. However, the reduction in surcharge for the Locke Lake and Birch Hill customers will be substantial, bringing the surcharge for Locke Lake customers down from $16.36 per month to $12.81 per month, and for Birch Hill customers down from $46.05 per month to $12.81 per month, representing a decrease of 22% and 72%, respectively. See Tab 12, Sch 5.

Q. Are there any other requests being made in this rate case that you believe will reduce the impact on PEU's customers?

A. Yes. As was I described above, PEU is asking the Commission to phase in the 5-year trailing average approach to establishing test period information. By implementing it in two phases, we were able to reduce the rate increase request by approximately 2.5%.

Q. Mr. Goodhue, in practical terms, what would be the impact on the average residential monthly bill if all aspects of PEU's proposed rate relief were approved by the Commission?

A. Overall, the average single family residential monthly bill is currently $62.68. Our requested rate increase would increase the average base amount in a customer's bill by approximately $13.48 per month, bringing the average monthly bill to $76.16. In addition to the impact on an average customer bill, it is important to note the specific impact on customers in the North Country systems, due to the elimination of the 4ccf minimum and the alteration of the surcharges. Currently, the average North Country system customer only uses 3.5 ccf per month, and as such, the impact on their bills from the elimination of the 4 ccf minimum would be a reduction in their monthly bill of $3.12 (at the current volumetric rate of $6.24/ccf), coupled with a reduction of $33.24 per month reduction in Birch Hill surcharge and/or $3.55 per month reduction in the Locke Lake surcharge.

VI. SUMMARY OF PROPOSED RATE RELIEF AND IDENTIFICATION OF PROPOSED MODIFICATIONS TO PEU'S RATEMAKING STRUCTURE

Q. Mr. Goodhue, would you please briefly describe the rate relief requested in this proceeding by PEU?

A. As is summarized above, with the filing of its full rate case documents as required by the Commission's administrative rules, PEU is requesting the Commission to approve, pursuant to its general permanent rate-setting authority, a rate increase of 20.35%, bringing its allowed revenues to a projected level of $8,452,006, as detailed in PEU's rate case filing at Tabs 12 and 13.

Q. Would you briefly describe the basis for this requested rate relief?

A. The fundamental basis for this request is that it represents the revenues required to cover PEU's current operating expenses and to meet the demonstrated costs of servicing PEU's direct debt obligations plus its share of the CBFRR. PEU has prepared its ratemaking schedules to demonstrate this fundamental basis.

Q. Is PEU also requesting a step increase in this proceeding?

A. Yes. To account for $964,350 of projected asset additions made in 2017, PEU will be seeking a step increase of approximately $79,017, or 1.15%. The requested increases will result in a combined total rate increase of approximately 21.50%.

Q. Is the rate increase the only relief that PEU is seeking in this proceeding?

A. No. As described above, PEU is also requesting that the Commission approve, pursuant to its general ratemaking authority, such modifications to the ratemaking methodology for PEU that it has approved for PWW in DW 16-806. PEU has filed its Petition for Further Modifications to Ratemaking Structure to affect this request in a formal manner. As described below, in order to provide a clear factual basis for the Commission's review of the proposed modifications, PEU has prepared its ratemaking schedules to reflect not only the operation of the current ratemaking method as established by the Commission in DW 11-026, but also operation of the modifications requested by PEU in its Petition under the methodology approved in DW 16-806. The rate increase being requested by PEU in this case is based on the DW 16-806 modified methods reflected in the ratemaking schedules.

Q. Why is PEU filing a rate case at this time?

A. PEU is filing a rate case at this time for a number of reasons. First, PEU has invested approximately $7.5 million in capital improvements and infrastructure replacements since the beginning of 2013, for which debt was raised in 2014, 2015 and 2016, and the current rates do not include the necessary dollars in the existing revenue requirement to fund the repayment of those debt instruments, for both principal and interest. Second, operating expenses of the Company have increased at or above the rate of inflation, as well as significant increases in property taxes consistently above inflationary levels, since the last filed permanent rate filing. In the case of property taxes, the Company does proactively process abatements for valuations that are deemed to be in excess of allowed or reasonable levels, given the current RSA allowing for the taxation of Utility Property as Real Property at both the State and Local level. As of the date of filing this case, the successful abatement of taxes for two communities served by PEU are included in the increases being requested, as a reduction to the increases filed for (as compared to the increases cited in PEU's Notice of Intent filed on August 16, 2017). Additionally, PEU has one local tax valuation that is in the process of being litigated, and if successful, the positive results that might be brought to bear from that proceeding will be reflected in the final rate increase requested at the conclusion of this case. Overall, the rate case being pursued at this time is necessary to provide for the ongoing cash flow needs to fund ongoing operating expenses and fund the repayment of debt obligations, as available to PEU in support of its ongoing obligations to its ratepayers.

Q. Please discuss the format of the ratemaking schedules filed by PEU upon which the requested rate relief is based.

A. PEU's requested rate relief is based on the modified ratemaking structure set forth in its filed ratemaking schedules. As further described in the testimony of Mr. Ware, these schedules embody financial information and resulting rates attributable to three distinct scenarios: (1) application of the modified ratemaking structure approved by this Commission in DW 11-026; (2) application of this modified ratemaking structure including the modifications described in DW 16-806; and (3) application of ratemaking models assuming that PEU were still an investor-owned utility. PEU's requested rate relief is based upon the DW 16-806 modified ratemaking structure.

Q. Mr. Goodhue, how do the rates resulting from applying the DW 16-806 modifications to PEU's ratemaking structure compare to the rates that would result from application of the existing modified ratemaking structure approved by the Commission in DW 11-026?

A. As indicated in Mr. Ware's testimony and on Exhibit DLW-1, Tab 12 (Customer Impact), the projected aggregate revenues estimated to be allowed under the current modified ratemaking methodology (DW 11-026) would be $7,780,092, a percentage increase over the test period revenues of 13.18%. In contrast, as shown on the same Exhibit, the projected aggregate revenues estimated to be allowed when the DW 16-806 modifications are applied (including proposed step increases attributable to 2017 additions) would be $8,352,108, a percentage increase over the test period revenues of 21.50%.

Q. If the current DW 11-026 methodology would result in a 13.18% increase, why are you asking the Commission to modify the methodology which results in a 21.50% increase?

A. As I described in my testimony above, PEU currently has lender covenants in place that it cannot meet and fully cover its cash flow obligations. This is because of the fact that PEU's depreciation lives are well in excess of its debt instrument lives, giving rise to the fact that the cash flow generated from depreciation does not fully meet the principal repayments on issued debt. Additionally, the new methodology is needed to: (1) insure adequate EBITDA coverage for PEU, as it relates to covenant requirements, (2) provide adequate cash flows from revenues to pay debt service, CBFRR and operating expenses, and (3) provide adequate support funds in the form of the RSF accounts, to provide for cash funding during times of revenue shortfalls and expense growth above inflationary levels between rate case filings. If PEU continues to operate under the current DW 11-026 methodology, the Company will become financially insolvent.

Q. How do the rates resulting from applying these proposed modifications to PEU's ratemaking structure compare to the rates that would have resulted assuming that PEU had remained an investor-owned utility, as it was pre-acquisition?

A. As indicated on Tab 12, Exhibit DLW-1 (Customer Impact), based on the assumptions stated in that exhibit, the projected aggregate revenues estimated to be required for a pre-acquisition investor-owned utility would be $8,545,800, a percentage increase over the test period revenues of 24.32%.

Q. Mr. Goodhue, can you provide a projection of how PEU's rates would increase under the proposed modified ratemaking methodology in the future?

A. The Company anticipates rates would increase at approximately the rate of inflation going forward. This is based upon the following assumptions: (1) the CBFRR revenues of the Company will remain at a fixed level until 2042, (2) normal operating expenses will increase at approximately the rate of inflation, (3) property taxes may continue to increase at rates of 5-8% per annum, and (4) the Company will be investing $1-1.5M annually on Capital and Infrastructure Improvements, at borrowed interest rates of between 2.5-4.5%. These increases would be implemented on an annual basis through the QCPAC surcharge for the debt service times 1.1, plus property taxes, on annual Capex spending, and then "trued up" for increases in operating expenses with rate cases filed about every 3 years, to reset permanent rates, and to refill or refund monies from the RSF accounts.

Q. How would these projected resulting rates compare to the rates that would likely have resulted under private ownership?

A. These rates would continue to be lower than rates under private ownership as a subsidiary of a publicly-traded investor owned utility. This is based upon the fact that the Company's cost of debt is only 2.5-4.5% currently, whereas under that ownership structure, PEU earned a ROE of approximately 16% pre-tax, on approximately 50% of its investments in infrastructure.

Q. Has PEU prepared a cost of service study in connection with this filing?

A. No. PEU is not seeking any change in rate design in this proceeding. There have not been any significant changes in the composition of PEU's customer base, and therefore PEU does not believe that a Cost of Service Study is required.

Q. Has PEU provided PEU's payroll figures?

A. PEU does not have its own employees. Instead it pays PWW a management fee under which PWW provides employee services to PEU. The management fee is shown in Tab 12 at Sch 1 Attach C, Page 2.

Q. Will PEU be seeking a temporary rate increase?

A. Yes. PEU will be seeking a temporary rate increase equivalent to 80% of the permanent rate increase being sought, exclusive of the Step Increase being sought for 2017 investments in capital assets. The basis for the temporary rate request is described in separate testimony to be offered jointly by Mr. Ware and me that supports PEU's Petition for Temporary Rates.

Q. Please describe PEU's efforts to communicate with the affected communities and customers relative to this filing.

A. Upon filing the NOI with the Commission on August 16, 2017, PEU communicated in writing with officials of all nineteen communities served by the Company. On August 17, 2017 letters were sent to Town Managers of all of the communities the Company serves, and on August 18, 2017 letters were sent to the entire slate of State Senators and Representatives for each of those communities. Accompanying the required notice to customers, which will be sent to customers in conformity with the regulations after this case is filed, we will be sending a Frequently Asked Questions ("FAQ") document providing information about PEU's rate increase request. This FAQ document is being prepared in three versions: one for Sunrise Estates customers only, one for Birch Hill and Locke Lake customers, and one for the balance of PEU's customers; this allows the company to properly address the 4ccf and surcharge topics on a more specific basis, for the affected customers to those particular elements of this filing. Finally, upon filing the NOI, PEU issued a press release about the NOI to news outlets that provide coverage in PEU's franchise area.

VII. REQUIRED APPROVALS AND CONSENTS

Q. Would you please identify any approvals and consents required to effect the rate relief and proposed modifications to PEU's ratemaking structure?

A. The principal approval required to effect the requested permanent rate relief and proposed modifications is the approval of this Commission under RSA 378:8 and :28. The requested rate relief and proposed modifications have already been approved by PEU's and Pennichuck's Board of Directors.

VIII. JUST AND REASONABLE FINDING AND CONCLUSION

Q. Mr. Goodhue, do you believe that PEU's proposed rate relief and application of the modifications to the ratemaking structure described in DW 16-806 will result in just and reasonable rates?

A. Yes. I believe the requested rates and the proposed modifications are just and reasonable for several reasons.

First, the requested rates, including the effects of the proposed modifications to PEU's ratemaking structure, are generally consistent with the long-term projections presented in DW 11-026, which assumed an average annual increase in rates of approximately 3% and with the fundamental premises underlying the Commission's approval of the City of Nashua's acquisition of Pennichuck and its utilities. While the rate increase requested in this proceeding, which reflects the cumulative revenue and operating requirements of four years with no permanent rate relief, is significant, when the cumulative increase is examined as an average annual increase, it is generally consistent with the original assumptions of the acquisition docket, giving consideration to the fact that property taxes have increased at a rate above levels contemplated at that time.

Second, the requested rates continue to be lower than the levels that are reasonably projected to result from continued private investor ownership under the pre-acquisition structure. This benefit to ratepayers, which was one of the principal reasons for the approval of the City's acquisition, is due in large part to the fact that PEU has been migrating to a utility that will finance all of its material capital needs by the issuance of debt, which results in a materially lower weighted cost of capital than a private investor-owned utility with a more traditional debt and equity capitalization.

Third, the requested rates are necessary to maintain PEU's ability to continue to provide safe and high quality water service, by financing continued reasonable and prudent operations and by having access to borrowed funds necessary to finance required capital assets and infrastructure.

Fourth, the requested modifications to PEU's current ratemaking structure are the result of a careful examination of the experience obtained through the prior two major debt financings completed for its sister subsidiary, PWW, as well as covenant compliancy issues experienced by both PEU and its parent Pennichuck Corporation. This experience has allowed PWW to develop the specific modifications proposed in DW 16-806 and further to have confidence that these modifications will enhance PWW, PEU and PAC the ability to access debt markets and/or term loans in the future at affordable interest rates and at reasonable covenants. In some ways, this experience was an important prerequisite to developing the specific proposed enhancements, which is why PWW pursued the modified rate structure first in DW 16-806, with the full expectation that this methodology would then be applied to both PEU and PAC in their next rate case filings.

Fifth, based on the ratemaking schedules filed by PEU as part of this rate case, the requested rates will demonstrably enable PEU to generate sufficient cash flows to support its ongoing operational and capital needs, as well as service its existing outstanding debt obligations.

Q. Mr. Goodhue, do you believe that the requested rate relief and adoption of the proposed modifications are required to ensure that PEU continues to be able to provide safe and high quality water service to its customers?

A. Yes. PEU's current ratemaking structure only provides a fixed coverage component in the revenue requirement for the repayment of principal and interest to the City of Nashua under the CBFRR. Without an equity return allowable to the Company, PEU does not have a rate structure that insures adequate cash flow coverage to cover all of its remaining operating expenses and the repayment of principal and interest on the balance of its debt obligations. This is further exacerbated by the fact that the cash flow generated from depreciation under the return on rate base is funded by assets with an average composite life of approximately 42 years, with some assets at 80 year lives. This cash flow is what is intended to provide the cash flow to repay the principal on debt used to fund the investment in rate base. However, the maximum life of debt available to PEU is 25 years, with a large portion of its debt instruments requiring repayment in 20 years. As such, the cash flow from depreciation is not nearly sufficient to cover the principal repayment cash flow requirements. Additionally, without the free cash flow generated by a return on equity, when PEU experiences reductions in revenue related to a wet year and a related reduction in outside irrigation, revenues are not sufficient to meet the fixed operating expenses of the Company. The cost of debt service for PEU, even at favorable interest rates to the long term benefit of ratepayers, coupled with the increase of operating expenses due to normal inflationary pressures, as well as increases above inflationary levels for certain expense items (i.e., State and local property taxes), has created a mismatch between the cash flow generated from a normal allowed rate of return and depreciation expense on rate base, to the coverage of the cash flow requirements of PEU's principal and interest payments and normal operating expenses. This inherent mismatch which exists for PEU under the existing ratemaking structure (as a nearly 100% debt financed entity), coupled with the regulatory lag of obtaining rate relief 12-18 months after a given test year, has created and will continue to result in the revenues allowed from traditional ratemaking being insufficient in generating the necessary operating cash flows required to cover all of the Company's operating expense and debt service needs, now and into the future. The requested rate relief and proposed modifications to PEU's ratemaking structure are precisely targeted to correct these deficiencies.

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

A. Yes, it does.