STATE OF NEW HAMPSHIRE

BEFORE THE

NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION

DW 17-___

Pennichuck Water Works, Inc.

Direct Testimony of Donald L. Ware

PWW0007-PWW0019

STATE OF NEW HAMPSHIRE
BEFORE THE
NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION

RE: PENNICHUCK WATER WORKS, INC.
DW 17- ___

2017 INTERIM QUALIFIED CAPITAL PROJECT ADJUSTMENT CHARGE FILING

DIRECT TESTIMONY
OF
DONALD L. WARE

NOVEMBER 22, 2017

<u>Professional and Educational Background</u>

Q. What is your name and what is your position with Pennichuck Water Works, Inc.?

A. My name is Donald L. Ware. I am the Chief Operating Officer of Pennichuck Water Works, Inc. ("Pennichuck" or the "Company"). I have been employed with the Company since April 1995. I am a licensed professional engineer in New Hampshire, Massachusetts, and Maine.

Q. Please describe your educational background.

A. I have a Bachelor in Science degree in Civil Engineering from Bucknell University in Lewisburg, Pennsylvania. I have a Master's in Business Administration from the Whittemore Business School at the University of New Hampshire.

Q. Please describe your professional background.

A. Prior to joining the Company, I served as the General Manager of the Augusta Water District in Augusta, Maine from 1986 to 1995. I served as the District's engineer between 1982 and 1986.

Q. What are your responsibilities with the Company?

A. As the Chief Operating Officer, I am responsible for the overall field operations of the Company, including water quality and supply, distribution, engineering, and customer service.

Q. What is the purpose of your testimony?

A. I will be providing details of the Company's interim Qualified Capital Project Adjustment Charge ("QCPAC") filing. This interim filing will present the QCPAC projects expected to be completed in 2017 and provide a calculation of the

QCPAC surcharge that the Company seeks to implement on or after March 1, 2018, subject to the approval of the New Hampshire Public Utilities Commission ("Commission"). This interim filing also presents the QCPAC projects proposed for 2018, and 2019.

Q. What is the authority for the Company's filing?

A. The Commission requested that the Company file an interim QCPAC program in Docket No. DW 16-806, by Order No. 26,070 issued on November 7, 2017.

Q. Why did the Commission request that the Company file an interim QCPAC filing?

A. The Commission approved the concept of an annual QCPAC in the order issued for DW 16-806. The purpose of the QCPAC filing is to allow the Company to recover annually the expenses associated with Qualified Capital Projects (QCPs) completed in the preceding year, and to present a forecast of the next three years of the Company's Board approved capital expenditures. The Commission requested the filing of this interim QCPAC filing to begin the process of this annual filing methodology, in order to capture QCPs for 2017, which were not included in the permanent and step increase rates in DW 16-806.

Q. What expenses associated with the Company's QCPs were envisioned in the settlement agreement as part of DW 16-806?

A. The settlement agreement proposed the recovery of the following expenses annually on Commission approved and audited QCPs completed in the prior year:

1. 1.1 times the annual principal and interest on the Bonds or other debt issued to fund the QCPs, and

2. The property taxes associated with the Company's investment in QCPs that were completed and used and useful in the prior year.

Q. Why is there a need for an interim QCPAC filing? Why not just complete the first QCPAC filing during the first week of February 2018?

A. Because there was no official QCPAC filing in the winter of 2017, the Commission did not formally review the Company's proposed 2017 through 2019 capital expenditures. Prior to the issuance of the Order under DW 16-806, the Company had a WICA surcharge pilot program in place, for which a filing had been made for 2017-2019, however this filing only captured a subset of all of the QCPs eligible under the QCPAC filing process. Pursuant to the Order issued under DW 16-806, the WICA program was terminated and replaced by the QCPAC. It is essential that the Company recover the funds which have been borrowed on a short term basis in 2017, to fund the QCPs completed in 2017. If the Company does not have a QCPAC in place in 2018, to allow the recovery of the expenses associated with QCP's completed in 2017, it will be in violation of its financial covenants, deficient of the needed cash flow to fund the repayment of this incurred indebtedness, and will be unable to issue bonds to properly fund these QCPs with long term debt over their useful lives or access its short term line of credit.

Q. Does the Commission have a starting point to work from in regard to this interim QCPAC filing?

A. Yes. The Company presented its Board approved 2017, 2018 and 2019 Board approved Capex projects, in addition to calculating the projected QCPAC surcharge of the Company completing those projects, in response to Staff Data Request 2-21 in January 2017, for the docket under DW 16-806.

Q. What was the Company's basis for projecting the impact of the QCPAC filing in 2018 on its revenue requirements?

A. The basis of the analysis was as follows:

1. The Company projected investing $9,787,000 in QCPs during 2017.

2. The Company projected selling bonds in March of 2018 to pay off the short term debt incurred during 2017 to complete these projects. The Bond was projected to be a 30-year note with an effective all in interest rate of 5.0%. The actual term and rate will not be finally determined until the bonds are issued to the market in 2018.

Q. What additional information is included in this interim filing that will bridge the gap between the issuance of the order in DW 16-806 and the first complete annual QCPAC process?

A. The Company has attached an updated Exhibit DLW-1, for the slate of 2017 capital projects that were presented in DW 16-806, Staff 2-21. The update provides an analysis of the additions and deletions to this January 2017 data response submission, along with an update with regards to costs and source of financing, as well as a projection of the QCPAC surcharge for the 2017 capital improvements.

The Company has also attached Exhibit DLW-2, which is a proposed timeline of the necessary submissions and processes which will be essential to transition from this interim QCPAC petition to the first official QCPAC petition filing, which is to be filed before March 15, 2018. The Company currently anticipates filing its first regular QCPAC petition during the first week of February 2018.

Q. What will the annual QCPAC filing look like?

A. The annual filing will present the slate of QCPAC projects that were filed with and approved by the Commission in the previous year and subsequently were completed and became used and useful by December 31 of the year immediately preceding the annual filing. The filing will present the calculation of the QCPAC surcharge to include the recovery of 1.1 times the total debt service (principal and interest) for the Bonds (or other debt) which shall be issued on or about March 1st, plus the estimated property taxes on the approved slate of QCPs from the previous year. The annual QCPAC filing will also include the Company's Board approved capital improvements program for projected capital investment to be made by the Company for the year of the filing as well as the two succeeding years. The Company, as part of the annual QCPAC filing, will be seeking the Commission's approval of a QCPAC surcharge for that previous year, as well as approval of the slate of QCPAC projects projected for the current year, and will provide for information purposes a review and commentary on the slate of QCPAC projects presented for the following two years.

Q. How do the projected 2017 capital additions presented in Staff DR 2-21 (DW 16-806) compare against the updated capital additions presented in this interim filing in Exhibit DLW-1?

A. The Company presented a slate of capital projects to be completed in 2017 in Staff DR 2-21 (DW 16-806) which projected $9,787,000 in capital expenditures.

Exhibit DLW-1 projects a revised slate of 2017 capital expenditures of $6,289,612, of which $4,498,943 will be bonded for in March of 2018 (with the remainder already funded by previously approved debt instruments in financing dockets before the Commission and as noted on Exhibit DLW-1), which is inclusive of funds the Company is looking to recover in the amount of about $89,000 in capital expenditures associated with the Commission approved SRF funding for the Amherst Street water main replacement project which was funded with $1,400,000 of NHDES SRF loan funds. This sum relates to an amount for the full borrowing for this project, over and above the amount already included in the Step Increase under DW 16-806. The sum of this SRF adjustment plus the anticipated bond issuance in March 2018 results in a total of $5,266,000 of Company projects which will be eligible for a QCPAC surcharge in 2018.

Q. Please explain why the Company's projected 2017 Capital expenditures are expected to be about $3.5 million less than was projected in January 2017?

A. The projected $3.5 million reduction in 2017 capital expenditures is due primarily to the following changes in projects or project scope:

1. Replacement of Brass meters with High Lead Content. The original budget projected a 2017 expenditure of $832,000 to replace over 2,300 meters. The Company is projecting the total expenditure for this project during 2017 will only be about $337,000, resulting in a reduction in capital expenditures in this area of about $495,000. A shortage in personnel staffing due to retirements, as well as time spent setting up new meters in Litchfield associated with the PFOA mitigation

project, were the primary reasons that the targeted number of replacements did not fully occur in 2017.

2. Information Technology Projects. The original budget projected 2017 IT expenditures of about $1,547,000, which was spread across a range of IT projects, the largest of which is the Company's ongoing Asset Management project, which was budgeted at $936,000 for 2017. The projected IT expenditures for 2017 will only be about $826,800, with $630,000 of that amount being dedicated to Asset Management. The result is a reduction in capital expenditures in this area of about $720,000, when compared against the Company's January 2017 projections. The majority of this difference is driven by projects that were purposefully differed due to a potential shortage of cash based upon management altering the timing of these projects, due to the timing of being able to receive the final order in DW 16-806.

3. The PWW-PEU interconnection project. This project had an original 2017 budget of $311,500. This project has been deferred into 2018 due to construction restraints placed upon work in the Merrimack River, associated with the NHDES permit for this project which was issued in late summer of 2017 (past the deadline for which construction could be started and completed during the statutorily allowed window of time to work within the river during the Summer construction season).

4. Snow Station Pumping Station upgrade. The original capex budget planned for the addition of a 3rd pump to the Snow pumping station to ensure the Company's ability to meet the demands in the Northwest High Pressure system.

This project was budgeted at $125,000. A detailed review and modeling of the Northwest High pressure system's peak demands, in conjunction with efficiency testing of the existing pumps, yielded the fact that there was not a need to add a third pump in the Snow Station in order to meet the flow demands of the Northwest High pressure system, in the near term. In lieu of adding a third pump, the existing pumps were rehabilitated to increase their efficiency and output, at a cost of $13,323, resulting in a reduction of about $122,000 of projected capital expenditures for 2017.

5. Replacement of Milford Booster Station. The replacement of the Milford Booster Station was budgeted at $550,000 in the original 2017 budget. This is a 25-year old booster station, which is a prefabricated, underground steel pumping station, with steel water pipes and two pumps. A detailed analysis of this station yielded the fact that both the station structure and piping were still in good condition and the pumps were operating efficiently, hence there was not a need to consider replacement of the station at this time. This project was deferred to an uncertain date in the future. This resulted in a $550,000 reduction in 2017's projected capital expenditures.

6. Improvements to the Northwest High Pressure System. The original 2017 Capex budget included $800,000 for improvements to the piping in the Northwest High pressure system. Due to various constraints, including available time to plan, design and complete this project in the current year, the Company did not complete the $800,000 of improvements to the Northwest High pressure system. These improvements have been deferred until 2019. .

7. <u>Replacement of Water Mains.</u> The Company projected spending about $4,428,000 on water main replacements, for unlined cast iron or steel water mains, which were reaching the end of their useful lives in 2017. The Company now projects the completion of about $2,000,000 of water main replacement/relocation projects during 2017, resulting in a reduction of about $2,428,000 in projected 2017 expenditures. The work that was projected to be completed, but was not completed, resulted from a combination of projects that were deferred. The deferrals were due to decisions by the City of Nashua and the Town of Amherst to delay certain 2017 calendar year projects into 2018, as well as the delay of street repaving on certain water main replacement projects from 2017 to 2018. As many of these projects are done in conjunction with sewer replacements and/or repaving projects within these communities, deferrals by them on those projects have a direct impact on the Company's ability to complete projects within a given year, versus deferring them in line with those other projects being completed by these other entities. Planning and completing main replacement projects such as this, in this manner, represents the most cost effective manner for the Company and its customers, as to overall cost of replacing the water mains, as certain costs can be shared with the other entities, and/or certain costs can be avoided by working in streets that are already going to be cut open for those other projects.

Q. What is the projected amount of revenue the Company is seeking for 2017 Capital projects that will be requested as a QCPAC surcharge in 2018?

A. When it files its first regular QCPAC petition in 2018, the Company will be seeking to fund 1.1 times the principal and interest and the property taxes associated with its investment during 2017, currently estimated to be about $5,266,000 of QCPAC eligible projects. The projected $5,266,000 of QCP's will be funded with:

1. A 30 year Bond in the amount of about $4,498,600 with an estimated 5% effective interest rate (or other equivalent manner of debt) issued in March of 2018,

2. The remainder of the SRF Bond approved for the Amherst Area Water Main replacement project in the amount of $767,357 with an effective interest rate of 2.46% and a term of 30 year.

The Company anticipates it will seek to recover approximately $474,000 in the form of a surcharge, to go into effect on or about March 1, 2018. The formal request for the 2018 QCPAC surcharge will be made in 2018 with the Company's full QCPAC filing which the Company currently anticipates will be filed in February 2018.

Q. Why is the Company seeking to recover a QCPAC surcharge on the Amherst Street Water Main Replacement project? Wasn't this SRF project funded via the step increase granted in DW 16-806?

Only the portion of this SRF loan that was associated with plant additions that were used and useful as of December 31, 2016 was recovered in the DW 16-806 step. The final total amount borrowed from the SRF loan for the Amherst Street Water Main project was $1,400,000, of which $632,643 was for used and used assets which were completed in 2016, and was recovered in the Step increase granted in DW 16-608. The Company is seeking 1.1 x principal and interest as well as the property taxes associated with the remaining and incremental $767,357 for work completed in 2017, borrowed through the SRF for this project.

Q. What is the Company seeking from the Commission in response to this petition?

A. The Company is requesting that the Commission accept this petition as fulfilment of the DW 16-806 order, which stipulated that the Company make a timely interim QCPAC submission. With the withdrawal of the WICA petition in DW 17-017, the Company is seeking approval of the slate of projects that will be completed in 2017 and will be the basis for a QCPAC surcharge petition in 2018, subject to an audit of the projects by the Commission and issuance of the Bond (or other equivalent debt) to pay for these 2017 projects and improvements. In addition, as is described in the Settlement Agreement and Order No. 26-070 in DW 16-806, the Company has provided the Commission with projects it anticipates for 2018 and 2019. No action is needed from the Commission at this time relative to the 2018-2019 projects.

Q. What is the current projected impact of the 2018 QCPAC surcharge on a typical single family residential bill?

A. Assuming the current 2017 projections are approved and are consistent with the final costs, the typical residential general metered customer using 103 CCF per year (8.58 CCF per month based on 2015 usage) will be $54.00 per month after the implementation of the Step increase granted in DW 16-806. The current estimate is that the QCPAC surcharge will result in a 1.50% increase to this bill, or approximately a $0.81 increase to the average monthly bill, resulting in a new monthly bill of $54.81 per month. This projected increase assumes that $5,266,000 of approved QCPAC projects will be approved and funded with a mix of debt as described above.

Q. Does the Commission need to approve a QCPAC surcharge with this Petition?

A. No. The QCPAC surcharge request for the 2017 projects will be made in 2018 when the Company files its first full QCPAC petition. This interim QCPAC petition is being filed now to seek approval of the Company's 2017 projects due to the timing of the Commission's Order in DW 16-806 and due to the requirement in the Order that the Company withdraw its DW 17-017 WICA filing, which was the vehicle for the Commission to approve the 2017

Q. Does this complete your testimony?

A. Yes.