STATE OF NEW HAMPSHIRE

BEFORE THE

NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION

Pennichuck Water Works, Inc.

Petition of Pennichuck Water Works, Inc. for Financing Approval

DW 20-_____

DIRECT TESTIMONY OF LARRY D. GOODHUE

April 23, 2020

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I. INTRODUCTION

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

A. My name is Larry D. Goodhue. I am the Chief Executive Officer of Pennichuck Water Works, Inc. (the "Company" or "PWW"). I have been employed with the Company since December 2006. I also serve as Chief Executive Officer, Chief Financial Officer, and Treasurer of the Company's parent, Pennichuck Corporation ("Pennichuck"). I am a licensed Certified Public Accountant in New Hampshire; my license is currently in an inactive status.

Q. Please describe your educational background.

A. I have a Bachelor of Science degree in Business Administration with a major in Accounting from Merrimack College in North Andover, Massachusetts

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 in several companies.

Q. What are your responsibilities as Chief Executive Officer of the Company, and Chief Executive Officer, Chief Financial Officer and Treasurer of Pennichuck?

A. Including my primary responsibilities as Chief Executive Officer, with ultimate responsibility for all aspects of the Company, I am responsible for the overall financial management of the Company including financing, accounting, compliance and budgeting. My responsibilities include issuance and repayment of debt, as well as quarterly and annual financial and regulatory reporting and compliance. I work with the Chief Operating Officer and other members of the Company's senior management team to determine the lowest cost alternatives available to fund the capital requirements of the Company, which result from the Company's annual capital expenditures and its current debt maturities

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 Pennichuck East Utility, Inc. – DW 12-349, DW 13-017, DW 13-125, DW 14-020, DW 14-191, DW 14-282, DW 14-321, DW 15-044, 16-234, DW 17-055, and DW 17-157, DW 18-101, DW 18-132, DW 19-112, and DW 19-069;
- Financings for Pennichuck Water Works, Inc. – DW 14-021, DW 14-130, DW 15-046, DW 15-196, and DW 16-236, DW 17-183, DW 18-133, and DW 19-026;
- Financings for Pittsfield Aqueduct Company, Inc. – DW 15-045, and DW 16-235, and DW 18-033;
- Permanent and Temporary Rate Increase Proceedings for: Pennichuck Water Works, Inc. – DW 13-130; DW 16-806 and 19-084; Pennichuck East Utility, Inc. – DW 13-126 and DW 17-128; and Pittsfield Aqueduct Company, Inc. – DW 13-128.

II. PURPOSE OF THIS TESTIMONY AND BACKGROUND OF THE PROPOSED FINANCINGS

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to explain PWW's request for approval and authority to issue up to $75,000,000 in aggregate principal amount of tax-exempt or taxable bonds for the following purposes:

(1) To finance $5.5 million in monies needed to complete a "one time" replenishment of the MOERR RSF for the Company back to its authorized imprest value. As described later in my testimony, this is essential to fully replenish that portion of the Company's RSF funds to its full imprest value at this time, as well as support or improve the Company's credit rating, which in turn gives the Company the opportunity to borrow at the lowest possible cost for its customers. This request is closely tied to the Company's rate case, Docket DW 19-084 which, if approved, will help ensure this is a "one time" replenishment of the MOERR RSF.

(2) To refund and refinance the currently outstanding Series 2014A and 2015A tax-exempt bonds and the Series 2015B taxable bonds. This will replace more than $56 million of existing debt with lower interest rate bonds on an extended term of repayment, resulting in annual cash flow savings with level overall debt service, as a direct pass-through savings to customers.

(3) the refinancing of the currently outstanding note payable to American United Life Insurance, which matures on March 1, 2021. This will replace approximately $2.4 million in existing debt with lower interest rate bonds for a newly re-established term of repayment, again resulting in direct savings to customers.

(4) funding of the overall cost of issuance for the bonds to be issued for all of the items included immediately above, as well as give overall authority to encapsulate those costs, as well as the authorized additional capacity to allow for the possibility that the bonds will be issued at either a discount or a premium in the market, in order to secure the necessary actual funds for items 1 thru 3 immediately above.

Q. Did you supervise the preparation of the Company's petition for authority to issue long term debt?

A. Yes.

Q. Does the Company have on file with the Commission a certification statement in its Annual Report with respect to its book, papers and records?

A. Yes.

Q. Mr. Goodhue, before explaining the details of the proposed financings, would you like to provide some history regarding the ownership of PWW and how that history supports this request for financing approval?

A. Yes. Currently, PWW is a wholly owned subsidiary of Pennichuck, which is, in turn, wholly owned by the City of Nashua, New Hampshire (City). The City 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, Pennichuck's shares were traded on a public stock exchange. This change in the ultimate ownership of PWW's parent, Pennichuck, from publicly traded shareholder ownership to ownership by the City has had important consequences for the operation of PWW.

One of the consequences is that PWW, after the City's acquisition of Pennichuck, no longer has access to private equity markets as a method of financing its capital needs. As contemplated by deliberations during the Commission's proceeding to approve the City's acquisition of Pennichuck in DW 11-026, after the acquisition, PWW expected to finance its on-going capital needs entirely through the issuance of debt. One result of this anticipated debt financing is that the weighted average cost of PWW's capital is significantly lower than it was prior to the City's acquisition. This lower cost of capital has direct benefits for PWW's customers. Under the docket for DW 16-806, the Company provided support for its existing capital structure, for which approval was granted for a modified rate setting methodology in Order No. 26,070. This financing petition is directly related to the Company's current debt needs, as well as a structure that is in full support of that modified rate methodology.

Q. Mr. Goodhue, how did the 2014 and 2015 Bond financings improve PWW's capital structure consistent with this history of the City of Nashua's acquisition of Pennichuck?

A. The 2014 and 2015 Bond financings may be viewed as the first and second steps in migrating PWW's capitalization to a format that was better aligned with the change in Pennichuck's ultimate ownership from private shareholders to the City. These financings accomplished a couple of favorable results. First, the new bonds were issued pursuant to loan documents that have financial covenants that are better aligned with the new ownership structure and presented less risk of future covenant violations. Second, the financings refinanced prior bonds, that were interest only and were subject to “balloon” payments at maturity, with bonds that are fully amortizing, such that PWW became less subject to risks in which it might not be able to raise funds under uncertain future market conditions to meet the “balloon” payment obligations.

Additionally, as a result of the 2014 and 2015 financings, all seven series of tax-exempt bonds that were in existence as of the date that the City acquired Pennichuck Corporation were refinanced. These bond series were all interest only with “balloon” maturity bond issuances, with covenants that were established in support of PWW’s then existing debt/equity funding model. The 2014 and 2015 refinancing activities allowed PWW to accomplish the following: (1) refinance the seven series of bonds with fully amortizing tax-exempt bonds, thereby effectively eliminating the previously identified future refinance and interest rate risk associated with those borrowed monies; and (2) allow these refinance amounts to have covenants which are much better aligned with PWW’s current capital structure.

Q. How were the 2014 and 2015 financing transactions viewed by rating agencies?

A. As a part of the financing petition process pursued in 2014 and 2015, the credit rating agencies reviewed the financing transactions favorably, resulting in an increase in PWW’s credit rating to an “A” rating with a stable outlook up from the equivalent of a BBB rating (the Company was rated by Moody’s prior to this transaction, and had the Company as a Baa2; equal to an S&P BBB rating) for the last bond offering prior to this financing and the completion of the acquisition of Pennichuck Corporation by the City of

Nashua as approved under DW 11-026, with its associated modified rate structure for PWW. Subsequently, the credit rating agencies further enhanced PWW's credit rating as it related to the Company's 2018 and 2019 bond issuances to an "A+" rating, initially released with a stable outlook attached, but as of 2019, with a negative outlook.

Q. What impact did the modified rate methodology as approved under Order No. 26,070 (Docket DW 16-806) have on the Company's credit rating, and the long-term prospects for the Company to access low cost debt for capital projects and infrastructure replacement needs?

A. The modified rate methodology approved under Order No. 26,070 was considered to be the next essential step in the overall recapitalization of the Company, with rates set based upon the manner in which the Company funds and pays for its obligations. Additionally, the Order approved a structure that established portions of the aggregated Rate Stabilization Funds under each major component of the overall allowed revenue requirement. In initial discussions with the Company's Bond Underwriter's, as well as the independent credit rating agency (Standard and Poors – "S&P"), these factors were perceived as extremely positive by the credit rating agencies. However, one of the factors that remained as a critical credit concern for the rating agency was the Company's inability to effectively mitigate the overall risk associated with regulatory lag due to the lack of equity funding. While the new rate structure allowed the Company to recover certain increases in expenses between rate cases (*e.g.* QCPAC increases), the rate structure did not provide revenue coverage for normal increases in operating expenses between permanent rate case filings. The impact of this, as it relates to revenue coverage for expense increases between rate cases, has caused the RSF fund in support of the

MOERR portion of the Company's allowed revenues to become impaired significantly since the last approved rate increase in docket No. DW 16-806, and as such, S&P had issued a constant rating (A+) for the Company. The primary driver in S&P issuing a negative outlook related to that rating in 2019 was driven by the lower cash resources on hand to backstop revenues of the Company. As a result, and as discussed in greater detail later in this testimony, in April 2020 the Company was issued a downgraded in its rating to an "A" credit, but still with a negative outlook. This action by the rating agency, was once again, all related to the Company's overall liquidity position, and ability to maintain adequate liquidity on a consistent and ongoing basis.

Q. Mr. Goodhue, has PWW sought the assistance of any investment advisor in connection with the development of the proposed financings?

A. Yes. PWW is working with representatives of B.C. Ziegler and Company ("Ziegler") to develop the structure and terms of the Bond financing contemplated in this petition. Ziegler will be the underwriter in connection with the issuance of taxable bonds or tax-exempt bonds, through the New Hampshire Business Finance Authority, as contemplated by this proposal.

III. <u>DESCRIPTION OF PROPOSED FINANCINGS</u>

Q. Would you please briefly describe the financings contemplated by PWW's proposed financings, and primary needs being addressed by this aggregated transaction?

A. The overall need for this financing is based upon several key issues, and as it relates to current bond market metrics which allow it to be a favorable and achievable debt financing and refinancing:

(1) Replenish the MOERR RSF to stabilize or improve the Company's credit rating to ensure the Company is obtaining debt financing at the lowest possible cost: The need to fully replenish the Company's MOERR RSF fund at this time, in conjunction with the rate relief being sought in docket DW 19-084, currently in pendency with the Commission, and in conjunction with the acceptance and implementation of the MOES (Material Operating Expense Supplement) allowed revenue factor in that case. As has been stressed in the past with the Commission, as a debt-only funded entity, cash flow coverage is paramount for the Company (to remain as a financially viable entity) and its ratepayers, and tied directly in with that is the ability to both: (1) access the debt markets, and (2) attract the lowest cost of borrowings possible.

It is very important to note that in the Company's current annual bond issuance, which is in process at this time, as approved as a subset of the overall approval from docket DW 17-183, the Company has just obtained its most current credit rating from S&P. And, as has been explained to the Staff and OCA in the pendency of the rate case under DW 19-084, the Company's overall ability to maintain proper liquidity, in both its operating cash accounts, and as it relates to the values maintained in its RSF funds (and the ability to refill and maintain those in a timely and effective manner, on a consistent and ongoing basis going forward) is the highest risk factor that the Company contends with: (1) in its overall ability to issue debt in the bond markets, and (2) attract the lowest possible interest rates on that issued debt.

A year ago, with the Company's annual bond issuance, the Company maintained its "A+" rating with S&P, but they issued a "negative outlook," which was a downgrade from the "stable outlook" tied to its "A+" rating provided in the prior year by S&P. The most current bond rating received in April 2020 associated with the current bond issuance in pendency resulted in S&P downgrading the Company one credit rating level to an "A" rated credit, but still with the "negative outlook." To quote S&P in their public report attached to the current bond rating issued, it is vitally important to note the full breadth of this risk, as perceived by them and the bond markets, and the underlying rationale for <u>fully replenishing the RSF funds at this time with this financing petition filing, as well as the need for the MOES factor to be included in the current rate case under DW 19-084.</u> The following are direct excerpts from the S&P reports:

> *"The downgrade reflects our view of the utility's multi-year trend of thinning liquidity: PWW ended fiscal 2019 with $1.1 million in available reserves, equal to 21 days' operating expenses, down from $6.5 million or 142 days' operating expenses at the end of fiscal 2016."*

And

> *"The negative outlook means we believe there is a one-in-three chance that we could lower the rating over the next two years. The outlook also reflects the utility's thinning liquidity, all-in debt service coverage (DSC) that is sufficient but vulnerable, and uncertainty concerning the outcome of the current rate filing, which is expected to conclude in October 2020."*

And

"If we believe liquidity is likely to continue to decline, or if DSC erodes to insufficient levels by our calculations, we could lower the rating further in the next two years"

However

"We could revise the outlook to stable with a successful rate case approval through the PUC that results in replenishment of reserves to the indenture-allowed levels."

As such, it is vitally important to understand that the principal underlying factor for this credit rating downgrade and the continued negative outlook, is solely related to the Company's current liquidity position and its inability to reaffirm and maintain adequate liquidity on its balance sheet. Even though an "A" rating is still a very good investment grade rating, every movement up or down in the Company's rating affects both its ability to issue debt in the market, as well as determining its cost of interest on issued bonds. Although it cannot be determined with absolute certainty, as bonds are purely a market driven instrument subject to actual supply vs demand pricing at the time of issuance, the Company's investment bankers have indicated a movement of one step in the rating of the Company probably equates to about a 20-40 basis points (0.20-0.40%) in the overall interest rate. However, given today's volatile markets, this range is very unpredictable, and could be a wider or narrower spread, depending on market conditions at that time. And it is important to note that this is not the only critical factor in maintaining an adequate investment grade rating. As has been demonstrated in discussions, pricing and marketing with our Bond Underwriters in order to complete the Company's current annual bond issuance, which is in pendency as of the time of the filing of this petition, it is also very important to note that a strong rating (A or A+) is critical in a difficult market, as in the one we are currently experiencing. If for some reason the Company was downgraded more than one step (from A to BBB+, instead of from A to A-), for example, our Bond Underwriters have indicated that there is a great deal of uncertainty that the Company would be able to get this transaction or other bond issuances done in this or other similarly volatile financial environments. As such, this risk is far greater than just an interest rate fluctuation risk, but an overall risk of the Company's ability to access necessary debt funds to pay for ongoing capital projects and infrastructure replacement, to the current and long-term benefit of customers

As such, and based upon all of this, another key element in this overall financing request is the ability to procure $5.5 million of funds to refill the MOERR RSF to its full imprest level, as fully disclosed and delineated in the schedules in support of DW 19-084, and

(2) <u>Refinance and reduce the cost of over $56 million in existing debt with lower interest bonds on an extended term of repayment to the direct benefit of existing customers</u>: Taking advantage of current market rates for bonds in refinancing certain of the Company's currently issued bonds, at more favorable "all-in" rates.

Specifically refinancing the Company's Series 2014A (remaining outstanding principal of $36,695,000), Series 2015A (outstanding remaining principal due of $18,330,000) and Series 2015B (outstanding remaining principal due of $1,625,000) bonds. These bonds were originally issued as tax-exempt bonds (2014A and 2015B) or taxable bonds (2015B) with an overall serialized maturity of 30 years, in their years of issuance. As such, the 2014 bonds have a remaining overall maturity of 24 years and the 2015 bonds have a remaining overall maturity of 25 years. And, as the 2014A and 2015A bonds were issued as tax-exempt private activity bonds, they are not eligible to be advanced refunded. However, private activity bonds may be advance refunded (the ability to refinance prior to maturity or a pre-specified "call date") with taxable bonds. As such, the Company is seeking to refinance these debt obligations with taxable bonds at this time, to take advantage of favorable interest rates (current rates are approximately 50 basis points below the rate on the current bonds, as demonstrated on page 2 of LDG-2, in the attached exhibits), and the ability to refinance these obligations for an additional 35 years, which combined together create a lower annual total debt service requirement, as included in the Company's DSRR allowed revenue buckets. This would extend the overall term of the debt, inclusive of the years already elapsed, plus the refinance term to be in essence, 41 years and 40 years, respectively for the 2014 and 2015 debt issuances. And, the refinancing would encapsulate the ability for the Company to defease the tax-exempt bonds in advance of their allowable "call dates" which are 10 years from the original date of issuance, and

(3) Reduce the cost of approximately $2.4 million of debt with American United Life Insurance (“AULI”): The Company has a note payable to AULI that was originally taken out in 1996 (to fund capital projects at that time) for $8 million, over 25 years, at an interest rate of 7.4%, with annual sinking fund payments of $400,000, and a “bullet” maturity due 3/1/2021 for $2.4 million. This debt instrument also has a “make whole” provision if it is repaid prior to that March 1, 2021 maturity date. This debt must be refinanced on or before 3/1/2021, as the Company does not possess the incremental cash on hand to pay the bullet maturity at termination, absent refinancing this obligation. Refinancing this obligation prior to today would have had a severe negative impact, as the “make whole” value was far in excess of a reasonable sum of money (approximately $811,000 when tested for possible refinance in March 2016). At this juncture, the “make whole” value, if paid off in the October 1, 2020 timeframe, would be approximately $53K (and approximately $74K if paid off as early as the August 1, 2020 timeframe), which when combined with the overall benefit of refinancing this debt for a new term looking forward at interest rates less than half the existing 7.4% rate, is highly beneficial for the Company and its ratepayers. This is especially important, as refinancing this amount ($2.4 million) on its own in early 2021, would not inure the same benefits as combining it into this overall financing, as that amount on its own is too small to take to the bond markets, and would be at much higher interest rates with onerous covenants and requirements,

if refinanced with a term loan at a commercial bank or the existing AULI lender; and

(4) Overall this will allow the company to re-term both the AULI debt and the 2014/2015 bonds to a full term of the debt maturities much better aligned with the overall lives of the underlying financed assets. The new bond issuance, including all of the financed and refinanced amounts, would be issued with a serialized bond issuance, up to 35 years. The portion used to refinance the AULI debt would be financed over 25 years as a part of the serialized offering, whereas the 2014/2015 bond escrow and refinance amounts and the RSF funds would be financed over 35 years. The overall impact of this is much better aligned with the overall concept of generational equity (as opposed to generational inequity), as the overall weighted average lives of the debt would be much better aligned with the current average estimated lives of the Company's P,P & E assets, which have a current weighted average depreciable life of approximately 39 years. And, the weighted average useful lives of the asset underlying the 2014 bonds, when issued, was 47.94 years, whereas the weighted average useful lives of the assets underlying the 2015 bonds, when issued, was 48.84 years.

These approximate principal amounts are exclusive of additional amounts that might require financing in connection with the Plan, including funding issuance costs, arbitrage escrow deposits, the AULI "make whole," which have either already been discussed in this testimony, or will be discussed later in this testimony.

A. <u>TAX-EXEMPT OR TAXABLE BONDS</u>

Q. Mr. Goodhue, would you please describe the proposed financings in more detail?

A. The financing will be accomplished by issuing Taxable bonds with a fixed interest rate, applicable to each instrument comprising the overall serialized bond offering. The term of the Bonds will be no greater than 35 years. Repayment of the Bonds will be unsecured, as per the existing Bond Indenture and consistent with all prior bond issuances since 2014. Based upon market conditions existing as of the date of this testimony, PWW believes that Bonds, with terms and conditions similar and aligned with the Company's already issued 2014-2019 Bonds, could be currently issued at an interest rate of between 3.5% and 4.5% percent per annum, with a goal of an overall average TIC (Total Interest Cost) approximating 3.67%, subject to PWW's credit rating and overall market conditions at the time of issuance. However, if PWW gets a credit rating enhancement as part of this Bond issuance process due to the improvement in the Company's liquidity and ability to maintain that liquidity resulting from this financing transaction and the results of the DW 19-084 rate case, an improvement in these bond interest rates could occur. Conversely, the impact of COVID-19, as well as the crude oil market and the likely possibility of a recession, on the U.S. Economy and the overall taxable bond market may have the opposite impact, as it pertains to bond rates, as impacted by the overall reaction to the issuance of taxable bonds into the markets, when the Company plans to issue them in the Fall of 2020. The rates for Taxable Bonds in the marketplace are not only impacted by the Company's bond rating, but also by supply versus demand pressures on those debt instruments, as it pertains to all bond issuances brought to the market at that time. As described below, PWW is providing as an exhibit to this testimony **(LDG-3)** which is a proforma financial projection of total debt service from this transaction, compared to existing debt service on the impacted refinanced debt instruments described above, along with the issuance of the $5.5 million of new money for the RSF funds, thru 2055 (the full horizon for the repayment of 35 years bonds issued for 2020). This exhibit has also been included as a response to Staff Tech Session Data Request 3-10 in the PWW rate case under docket no. DW 19-084. Among other assumptions, this model assumes that the Bonds will be issued at an overall TIC of 3.67%. The key points to understand from this exhibit are: the net P&I savings earned in year-one of coming out of this refinancing activity, the net P&I savings earned in each year leading up to the original maturity date years of the refinanced 2014/2015 bonds, and the fact that the overall P&I of the new bonds in the years after those years reflect a total debt service which remains essentially consistent and at levels that are at or below the total debt service leading up to those years. This is vitally important, as the Company's allowed revenue in its rate structure from DW 16-806 is tied to cash coverage for the P&I payments related to the Company's debt obligations, and as such, maintaining or reducing the cash needs for those payments going forward is the ultimate goal in those out years. In essence, this financing, as a subset of the full DSRR portion of allowed revenues in those future years, represents a stabilization or savings to rate payers as a component of allowed revenues from the DSRR portion of the Company's revenue requirement.

Of course, the actual financing structure, rates, terms and conditions, amount, redemption provisions and coupon rate of the Bonds would be determined at the time of issuance based upon market conditions at that time and the Company's credit rating at the time of the issuance of these bonds.

Q. What are the covenant requirements for this portion of the proposed financing transaction?

A. The new debt is to be issued under the loan and trust agreement which was adopted for the 2014 and 2015 tax-exempt bond financings. PWW intends to issue this new debt with the covenants set forth in that Loan and Trust agreement which were implemented to be best aligned with PWW's current capital structure and its current and existing modified rate structure approved in Order No. 26,070.

Q. When does PWW intend to issue the Financing Bonds and complete this portion of the financing transaction?

A. PWW intends to issue the Financing Bonds on or before October 1, 2020 (preferably as early as September 1, 2020). PWW and the settling parties to the rate case wish to apply any cash flow savings from this financing transaction to customer rates. Resolution of the total debt service from this financing is instrumental to the included MOES factor in that rate case, and as to whether the MOES will be able to fully support or replenish the MOERR RSF on a going forward basis.

Additionally, the Company and its investment bankers consider it to be extremely important that this bond issuance be completed prior to the 2020 Presidential Election, as the impact of the results of that election upon the financial markets in the U.S. would most likely add another layer of uncertainty as to the overall cost and ability to issue these bonds, during or after the election. As such, the Company is filing the petition seeking an Order NISI, and is hopeful it could obtain approval for this financing no later than June 30, 2020 (or soon thereafter), allowing for the public comment period that follows the issuance of such an order, and in order to complete this financing as soon as practical on or before the dates specified above, and giving full visibility to the results of the financing as they are attributes to the completion of the rate case under docket DW 19-084. As a rule, it takes 5-8 weeks to complete the entire process of documenting, processing, marketing and closing upon a bond issuance to the markets, and the Company would anticipate beginning that process as soon as the Order NISI was received, and in parallel with the expiration of the public comment period. This would allow the Company to complete the bond issuance on or about September 1, 2020.

B. OTHER ASPECTS OF THE PROPOSED FINANCINGS

Q. Please explain how the Bonds would be issued through the New Hampshire Business Finance Authority.

A. The Bonds would be issued and sold by the New Hampshire Business Finance Authority ("NHBFA"), subject to approval of the NHBFA, and the Governor and the Executive Council. This is a requirement if they are to be issued as Tax-exempt bonds under the Private Activity Bond rules, as currently exist under the IRS code, but also essential for the issuance of the Taxable bonds. In order to issue the Taxable bonds to the market directly by the Company, PWW would be required to obtain its own CUSIP number and undergo the costly and lengthy process of meeting all of the requirements of the "blue sky" laws as established and required by the Securities and Exchange Commission and each state where the bonds would be offered, in addition to drafting a new bond indenture. A new bond indenture would be cost-inefficient and may require implementation of intercreditor agreements for all of the Company's already issued bonds.

These bonds will be issued by NHBFA as one or more series under the 2014 Loan and Trust agreement which was agreed and entered into by: the NHBFA, PWW and the Trustee. All payments of principal and interest on these bonds would be limited obligations of the NHBFA and would be payable solely from payments made by PWW. These bonds would not be general obligations of the State of New Hampshire, and neither the general credit nor the taxing power of the State of New Hampshire or any subdivision thereof, including the NHBFA, would secure the payment of any obligation under the bonds.

Q. Will this proposed financing require PWW to update its credit rating with the rating agencies?

A. Yes. PWW, with representatives of Ziegler, will meet with Standard and Poors ("S&P") to update PWW's current credit rating prior to the issuance of the proposed debt obligations. Arrangements would be made to meet with the S&P within the 5-8 period needed to issue the bonds, as described above. The S&P bond rating would be issued in the correct timeframe preceding the issuance of the bonds to the market. This review by S&P must be conducted contemporaneously with the issuance of the bonds and cannot be completed prior to that timeframe. This is an essential step in the process of issuing these financial instruments and is highly impactful upon the Company's ability to issue the bonds and secure a favorable cost of interest on the bonds.

Q. Will PWW be required to establish and maintain a Debt Service Reserve Fund to support the issuance of the proposed debt obligations?

A. PWW does not contemplate that a statutorily required Debt Service Reserve Fund ("DSRF") will be required to support issuance of the Bonds. Based upon PWW's current credit rating, and the bond market's willingness to purchase its 2014, 2015, 2018, 2019 and April 2020 bonds without a DSRF, PWW does not expect that a DSRF will be required for this financing activity. Additionally, the modified rate structure approved under DW 16-806 on Order No. 26,070, enhanced PWW's cash flow certainty in support of the repayment of its debt obligations (specifically the DSRR 1.0 and DSRR 0.1 elements of the Company's rate structure), coupled with the modified and bifurcated Rate Stabilization Fund structure approved in the order (again, specifically the DSRR RSF element of the Company's rate structure). And, the process being pursued for the inclusion of the MOES in the current rate case under DW 19-084, along with the $5.5 million of new money to fully re-establish the RSF sub-funds to their full imprest values, further adds credence to the case that obviates the Company's need to provide for a statutorily required DSRF, as defined by the regulations under the IRS code.

Q. What are the estimated issuance costs for the debt obligations contemplated by this Finance Plan?

A. The estimated cost to issue the debt obligations for the Bond portion contemplated by the proposed financings will depend, in part, on the final structure of the proposed financings, including whether tax-exempt or taxable bonds will be issued. As of the time of this testimony, PWW expects that the customary costs of issuance, including legal and underwriting costs, and the NHBFA fees, will be approximately $1,200,000-$1,300,000 in the aggregate. These estimated amounts are being included, in addition to the total $71.6 million of principal being financed/refinanced, as the amount applied for as a reservation of funds accessible thru the NHBFA, as a part of their overall preliminary approval of this financing transaction. The application and approval from the NHBFA are being pursued concurrently with this petition filing, in addition to the other approvals already received and/or required by the Company to complete this transaction. In the Exhibits attached to this testimony, approximately $1.28 million in COI has been included in those proforma schedules: LDG-1 (balance sheet – assets, deferred charges, equity and liabilities), LDG-2 (operating income statement.

Q. How does PWW intend to treat these new debt issuance costs for accounting purposes?

A. PWW intends to amortize the issuance costs of the proposed financings on a straight-line basis over the terms of the newly issued bonds. This amortization proposal is consistent with the methodology applied with respect to issuance costs in previous financings by PWW.

IV. <u>REQUIRED APPROVALS AND CONSENTS</u>

Q. Mr. Goodhue, would you please identify any approvals and consents required to consummate the transactions contemplated by the proposed financings?

A. In order to consummate the transactions contemplated by the proposed financings, the following approvals and consents are required:

(1) the requested approvals and findings of this Commission required by RSA Chapter 369;

(2) approval by the NHBFA and the Governor and Executive Council to issue taxable bonds thru the NHBFA;

(3) authorization by PWW's Board of Directors;

(4) authorization by Pennichuck Corporation's Board of Directors; and

(5) approval by the City of Nashua, in its capacity as Pennichuck's sole shareholder.

Q. Please describe the status of these approvals as of the date of this testimony.

A. PWW and Pennichuck's Boards of Directors have already provided preliminary approval for the proposed financings under this petition and have authorized management to pursue all steps necessary to complete the transactions. A copy of these approval actions is attached to this testimony as **Exhibits LDG-6 and LDG-7**. PWW's Board of Directors will also approve the final structure and terms of the proposed financings and the Bond Purchase Agreement, pursuant to which the proposed bonds will be issued, and other material documents and agreements when such documents are finalized.

PWW is preparing concurrently with this filing, a request for approval to the City of Nashua. It is anticipated that this request will be considered by the Board of Alderman during their two meetings in the month of May 2020 and remanded to the City's Special Water Committee between those two meetings for consideration and recommendation for passage back to the full Board of Alderman in the subsequent full meeting of the Board.

Also concurrent with this filing, PWW is submitting its application to obtain preliminary approval by the NHBFA Board of Directors to issue taxable and/or tax-exempt bonds on behalf of PWW. It is anticipated that this application will be considered and voted upon during the NHBFA's May 2020 meeting. Upon receiving approval from the NHBFA, and the subsequent approval of the Governor and Council on this request, this will be provided to the Commission in support of this petition. The NHBFA has not actually reserved any portion of its bonding limit at this time, as it awaits the Company actually receiving authority to issue the bonds from the NHPUC from this financing petition filing, and is thereby able to make a firm commitment to purchase/issue the bonds thru the NHBFA. PWW expects the NHBFA Board of Directors will take final approval action with respect to the proposed plan sometime during the next few months, as a part of this overall approval process, and PWW will provide a copy of this action to the Commission as soon as it becomes available.

It is important to note that all normal processes for obtaining these approvals at the City of Nashua, the NHBFA, and the Governor and Council, are currently being handled in non-traditional ways, given the constraints and limitations imposed on those processes by the COVID-19 pandemic emergency protocols in place within the State of NH.

Q. Mr. Goodhue, when would PWW expect to be able to consummate the transactions contemplated by the proposed financing?

A. As of the date of this testimony, PWW expects to obtain all necessary approvals and consents, and satisfy all other conditions to closing the proposed financing, to allow closing on the transactions on or before September 1, 2020, but no later than early to mid-October 2020.

Q. When does PWW need to receive the Commission's approval of the financings contemplated by the proposed financing?

A. For the reasons described in this testimony, including the desire to consummate the transactions as soon as possible, and in light of the timing for which this process is directly impactful on the rate case in pendency under docket DW 19-084, which includes the approval of the MOES factor, PWW respectfully requests that the Commission issue an Order NISI no later than June 30, 2020, with a public comment period of 30 days, or less, if at all possible.

V. DESCRIPTION OF ATTACHED SCHEDULES

Q. Please explain Schedule LDG-1, entitled "Balance Sheet for the Twelve Months Ended December 31, 2019".

A. Schedule LDG-1, pages 1 and 2, presents the actual financial position of the Company as of December 31, 2019 and the pro forma financial position reflecting certain adjustments pertaining to the proposed $71.6 million Bond financing, the replenishment of the RSF funds back to their full imprest levels, as well as the estimated cost of issuance related to the financing.

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

A. Schedule LDG-1, page 1, reflects the pro forma adjustments to record overall impact on the RSF fund and Bond Project fund sections of the financial statements as it relates to the refinancing and financing of the debt instruments included in this transaction, as well as the cost of issuance from the transaction, and the funding of the escrow deposits for the advanced refunding of the 2014/2015 bonds. Schedule LDG-1, page 2: This schedule reflects the impact on the Long-term Debt section of the balance sheet, and also reflects the income impact on retained earnings related to costs associated with the financings, as reflected on Schedule LDG-2. Schedule LDG-1, page 2, also records the use or transfer of intercompany funds to support some of the related expenses, to the extent they are needed.

Q. Please explain Schedule LDG-2, entitled "Operating Income Statement for the Twelve Months Ended December 31, 2019".

A. Schedule LDG-2 presents the actual operating income statement of PWW for the year ending December 31, 2019, and the pro forma income statement reflecting adjustments pertaining to the proposed financing.

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

A. Schedule LDG-2 contains three adjustments to develop a pro forma income statement reflecting the proposed financings. The first adjustment records the estimated change in interest expense resulting from the financings (including refinancings). The calculation of the net interest adjustment is shown on page 2 of Schedule LDG-2. The second adjustment records the incremental amortization expense from the costs of issuance for the financings. And lastly, the third adjustment records changes to income tax expense result from the additional interest expense, assuming an effective combined federal and state income tax rate of 27.08%. It is important to note that even though the impact on the income statement as shown on this schedule is overall quite immaterial, the overall cash savings in the first year, as shown on Schedule LDG-3 is approximately $970,000 at the 3.67 TIC level. This coupled with the DSRR 0.1 factor (approximately $97,000) in the Company's rate structure results in over $1 million is savings for rate payers to existing permanent rates, or as a component of rates being sought in docket DW 19-084 and shown on the proforma Sch A as submitted with the responses to Staff Tech Data Requests set 4, and as attached as Exhibit LDG-8 to this testimony.

Q. Please explain the forecast data presented on Schedule LDG-3.

A. Schedule LDG-3 sets forth a long-term proforma projection of the differential in total annual debt service cash requirements from this transaction for PWW over a 35-year period from 2021 to 2055, based on estimates and assumptions, and reflecting the effects of the financings contemplated by the proposed financings. This is the same analysis supplied as the response to Staff Tech Data Request 3-10 in PWW's rate case in docket DW 19-084.

Q. Can you explain the need for the escrow deposit on the 2014 and 2015 bonds being refinanced, what that current cost is, and how it is beneficial overall for ratepayers?

A. The escrow deposit is the amount required to fully redeem the prior bonds within 90 days, on their respective future "call" dates. The escrow will be invested in U.S. Treasury State and Local Government Series ("SLGS") obligations or similar instruments, as per IRS rules, and as per the Company's currently existing bond indenture, in order to currently refund the 2014/2015 bonds prior to their future "call dates" in accordance with IRS regulations. This sum of approximately $6,973,050, as shown in the attached **exhibit LDG-4**, has a present value of approximately $2,350,000, the full value of which is completely offset by the annual debt service savings from this total financing activity, in the aggregate, by the third year of the serialized offering (as calculated on LDG-3 to be $2,937,567 (at the proforma 3.67 TIC rate), in addition to the continuation of annual debt service cash flow savings beyond year 3.

But, even more importantly is the fact that the refinance of the 2014/2015 bonds is actually what enables the Company to be able to refinance the maturing AULI debt at favorable terms, and the $5.5M replenishment of the RSF funds to their full imprest levels at this time. In referring back to the discussion earlier in this testimony about the impact on the Company's credit rating due to liquidity, and the impact that rating then has on borrowing rates, it is important to consider the following. As shown on the attached **exhibit LDG-5**, a movement of 30 bps (the average of the cited range of 20-40 bps earlier in this testimony) on the Company's issued bond interest rates, over the next 35 years, assuming $10M in annual capex and bond issuances, as either a reduction in the bond interest rate (if it allows the Company's bond rating to return to a higher level from this transaction and the MOES factor in the rate case, allowing for the re-establishment and ability to maintain an adequate liquidity position, or it avoids a further downgrade by S&P as indicated in the quoted text from the most current credit report), the overall savings in avoided interest cost on those aggregated issuances over the next 35 years is approximately $13 million (the savings at a 20 bps differential would still be approximately $8.7 million, whereas it could be as high as approximately $17.3 million with a 40 bps differential), and more than justifies the overall benefit in accomplishing this transaction at this time, including the funded escrow cost for the transaction. Thus, the combined effect of reducing the overall cost of existing debt and the stabilization or improvement of the Company's bond rating is a significant positive value to our customers. Although the requested refinancing will result in payment over a longer term, any long-term additional cost is outweighed by the long-term advantages and savings to customers, especially as it applies to the Company's currently approved allowed revenue structure, where the DSRR portion of those allowed revenues are directly tied to the annual cost of debt service on its outstanding and issued debt.

Q. Will the Company be preparing a long-term financial projection model in support of this bond transaction, like it has for past offerings of this type?

A. The Company will be preparing a long-term financial projection model, to be used as the basis of the credit review with S&P, and to insure compliancy with covenant compliance over the 35-year forward looking horizon. The Company is certain that this model will show a favorable outcome as compared to current forecast models, as the impact of this financing overall brings cash flow and total debt service savings to bear over the full 35 years looking forward. However, this model cannot be completed and prepared at the time of this filing, as there is an April 2020 bond issuance round currently in process as described earlier in this testimony, and the actual results of that issuance needs to be imbedded into the model, before the proforma impact of this new financing is layered into the model This updated model will be provided as a supplement this filing, once it can be updated and completed in early May, and will include in that projection the following three components:

(1) a Cash Flow Component;

(2) a Profit & Loss Component; and

(3) a Balance Sheet Component.

This form of projection model has been used by PWW, working with its investment bankers, to assess the impacts of its bond financing activities for the bonds issued in 2014 thru April 2020. This projection will demonstrate that, based on reasonable assumptions and projections regarding numerous variables including future revenues based upon the approved rate methodology from DW 16-806, inflationary forecast of operating expenses, interest costs, capital expenditures, and establishment of the new debt arrangements from this current petition, that PWW will continue to be able to provide necessary water service at reasonable revenue requirements and with satisfactory financial performance measures following issuance of the debt obligations contemplated by this proposed financing petition. Specifically, with respect to interest rates, this projection will make the conservative assumption that the Financing Bonds would be issued at an interest rate of 3.67%. While PWW has made this assumption for purposes of this long-term financial projection, PWW notes that, based on current market conditions prevailing at the time of this testimony, bonds with terms and conditions similar to the Bonds could be issued at rates different from this assumption, given the uncertainties in the economy and financial markets surrounding the impact of COVID-19 in the U.S., as well as other economic factors affecting the U.S. and global financial markets. Furthermore, this long-term projection will demonstrate that the proposed financings are consistent with the assumptions supporting the approval by the Commission of the City of Nashua's acquisition of Pennichuck in DW 11-026 and Order No. 25.929, as well as the modified rate structure approved under DW 16-806 and Order No. 26,070.

VI. PUBLIC GOOD FINDING AND CONCLUSION

Q. Do you believe that the issuance of up to $71,600,000 in aggregate taxable or tax-exempt bonds, as contemplated by the proposed financings is consistent with the public good?

A. Yes. As described earlier in this testimony, the proposed financings are consistent with the public good because they will:

(1) allow for the issuance of tax-exempt or taxable bonds which have repayment terms and financial covenants that are aligned with the capital requirements of

PWW as it is now ultimately owned by the City of Nashua, and supported by PWW's newly modified allowed revenue rate structure;

(2) refinance long-term debt with favorable interest rates and maturities that are better aligned with the useful lives of the originally funded capital assets, to the long-term benefit of PWW's ratepayers; and

(3) generally improve the capitalization of PWW consistent with the assumptions underlying the Commission's Order No. 25,292 (Approving Acquisition and Settlement Agreement) and providing for future revenue requirements for the DSRR portion of allowed annual revenues that will either be lower than current rates, and/or will maintain a level that is level in the years thru full maturity of the refinanced and re-termed bonds, based on reasonable projections.

(4) Result in savings to PWW's customers by reducing the principal and interest payments on the financial instruments that are being refinanced, as well as the estimated impact on the cost of money for future debt issuances.

(5) And, fully replenishes the necessary RSF funds on a "one time" basis, which are used to backstop the Company's allowed revenue structure, operating expenses, and overall liquidity position currently and going forward, to the overall long-term benefit to customers, as it allows the Company to adequately fund its capital projects and operations at favorable interest rates, and with full access to the debt markets.

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

A. Yes, it does.