

**STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION**

DW 08-086

EASTMAN SEWER COMPANY, INC.

**Petition for Financing Authority
and
Temporary and Permanent Rate Proceeding**

Order Approving Financing Request

ORDER NO. 24,967

May 21, 2009

APPEARANCES: Stephen P. St. Cyr & Associates, Inc. by Stephen P. St. Cyr for Eastman Sewer Company, Inc.; and Staff of the Public Utilities Commission by Marcia A. B. Thunberg, Esq.

I. PROCEDURAL HISTORY

Eastman Sewer Company, Inc. (ESC) is a regulated utility that provides sewer service to 533 residential customers and two commercial customers in the Town of Grantham. On June 24, 2008, ESC filed a notice of its intent to file rate schedules. On August 18, 2008, ESC filed revised tariff pages designed to increase its annual revenues by \$56,386, or 46.28%, over its current authorized level of rates. ESC requested that \$33,241 of the \$56,386 be applied to its capital reserve fund to finance system improvements.¹ ESC requested temporary rates and also requested authorization, pursuant to RSA 369, to borrow \$238,850 from either a bank or from the Eastman Community Association in order to finance system improvements. This loan would be for a ten-year term at an interest rate of 7%.

¹ ESC's capital reserve fund was established by the Commission in ESC's initial rate case, Docket No. DR 90-170. The Commission found that ESC was undercapitalized because the vast majority of the original sewer plant had been expensed for tax purposes, and thus the Commission ordered the establishment of the fund. The \$10,008 collected annually through customer rates is deposited to a separate account and is used exclusively for capital improvements. *Eastman Sewer Company*, Order No. 20,390, 77 NH PUC 93 (1992).

On September 18, 2008, the Commission issued Order No. 24,896, which suspended ESC's proposed tariff pages and scheduled a prehearing conference for October 29, 2008. On October 6, 2008, ESC mailed a copy of Order No. 24,896 to all of its customers.

On October 29, 2008, ESC amended its filing to increase the amount of its borrowing to \$344,534. ESC did not change any of the other proposed financing terms.

The Commission approved a procedural schedule by a Secretarial Letter dated November 5, 2008, which provided for a hearing on temporary rates on December 17, 2008. At the hearing, Staff and the parties presented a settlement agreement on temporary rates that the Commission approved by way of Order No. 24,927. The procedural schedule also provided for a hearing on ESC's financing request, which was held on April 16, 2009. At the hearing Staff and ESC presented a settlement agreement on the terms of the financing.

II. SUMMARY OF SETTLEMENT AGREEMENT

A. Financing Terms

Staff and ESC attached to the agreement a commitment letter from Lake Sunapee Bank to borrow up to \$380,000. Under the terms of the commitment letter, Eastman Community Association (ECA), the owner of ESC, will provide a guarantee of the loan, pending approval of the ECA Council at its June 27, 2009 meeting. ESC testified that at ECA's April 4, 2009 Council meeting, ECA indicated that it would likely vote unanimously to approve the financing at its June meeting. Hearing Transcript of April 4, 2009 at 13, lines 20-24 and at 14, lines 1-10. The loan is for a ten-year term and ESC will pay interest during the first year "construction phase" of the loan at a rate of prime minus one-quarter percent on any outstanding balance of funds drawn. This rate will be adjusted quarterly; as of March 24, 2009, the rate was 3%. For the remaining nine years of the term, ESC will pay interest at a fixed rate of 5.5% and will be

required to make monthly payments of principal and interest sufficient to retire the loan in full at the end of the nine-year period.

ESC testified that it needed the loan to pay for necessary capital improvements that it cannot otherwise fund from its existing rates and capital reserve account. 4/16/09 Tr. at 9 lines 4-11. Staff and ESC recommend the Commission approve the terms of this loan.

B. Use of the Proceeds

In March 2008, CLD Consulting Engineers completed an analysis of ESC's sewer system and provided recommendations for capital improvements. CLD recommended that ESC perform \$500,000 in capital upgrades and replacements over a period of several years. ESC stated that these upgrades are necessary due to the age of the sewer system and the need to meet current permitting requirements. Staff testified at hearing that it had reviewed the engineering consultant's report and had visited ESC's facilities and that it concluded that these improvements were clearly necessary. 4/16/09 Tr. at 17 lines 8-14. ESC plans to perform the most necessary improvements and cost estimates have been provided as follows: 1) West Cove B Pump Station, \$7,209; 2) Grinder, Influent Flowmeter and pH Meter, \$75,486; 3) Headworks Modification, including building, site work, and design engineering, \$135,192; 4) West Cove A pump station, pump replacement, generator and transfer switch, \$66,846; and 5) West Cove A overflow structure, \$59,800. ESC testified at hearing that the cost estimates contained in the settlement agreement were higher than those stated in ESC filings because the bids for the projects, in particular the headworks project, came in \$100,000 more than expected. 4/16/09 Tr. at 14 lines 20-24 and at 15 lines 1-5. Staff and ESC agree that these capital improvements are necessary for the provision of safe and adequate service, that they are necessary to bring ESC into compliance with permitting requirements, and that moving ahead with these upgrades at this time represents prudent utility management.

The proceeds of the financing are also intended to repay \$30,000 in short-term loans made by ECA to ESC. These loans were needed by ESC in order to fund its operations while ESC sought rate relief. Staff and ESC urge the Commission to find that the use of the funds for the improvements and repayment of the loan from ECA are consistent with the public good.

C. Rate Treatment of the Improvements

Staff and ESC agree that the rate treatment of the capital improvements to be acquired or constructed with this financing will be considered in the permanent rate phase of this proceeding. According to the approved procedural schedule, a settlement agreement, if proposed, was to be filed by the settling parties on or before May 15, 2009, to convey the recommendation of Staff and ESC. Staff and ESC anticipate they will recommend a permanent rate increase based on ESC's test year with the permanent rate increase to be reconciled with temporary rates. Staff and ESC also anticipate they will recommend a step adjustment to rates which will take into consideration the additional capital improvements to take effect once the capital improvements are completed and in-service.

III. COMMISSION ANALYSIS

Pursuant to the provisions of RSA 369:1, public utilities engaged in business in New Hampshire may issue evidence of indebtedness payable more than 12 months after the date thereof only if the Commission finds the proposed issuance is "consistent with the public good." Analysis of the public good consideration involves looking beyond the actual terms of the proposed financing to the use of the proceeds of those funds. See, *Appeal of Easton*, 125, N.H. 205, 211 (1984).

ESC seeks to borrow \$380,000 to finance capital improvements to its sewer system and repay a short-term loan from ECA. According to the commitment letter from Lake Sunapee Bank, the loan will be for a term of ten years, with the first year considered the construction

phase of the loan. During the construction phase, interest will be calculated at prime minus $\frac{1}{4}\%$ and adjusted quarterly. The interest rate for the remaining nine years will be fixed at 5.5%. As collateral Lake Sunapee Bank will hold a first security interest in all fees and assessments of ESC now due or to become due. A condition precedent to the loan is a guaranty from ECA. Origination fees for the loan have been waived and there is no prepayment penalty. Having reviewed these terms, we find them reasonable and consistent with loan terms the Commission has approved for other small utilities. We note that the interest rate is lower than other recently approved financings and we find that ECA's ability to obtain financing at this low rate will benefit customers.

As for the capital improvements that will be funded by the proceeds of the financing, ESC's consultant and Staff have determined that the improvements are necessary. Based on this evidence, we find that ESC has demonstrated that the capital improvement projects are necessary and will enable it to provide better service to its customers. As to the use of the proceeds to repay a short-term loan from ECA, we understand that the loan enabled ESC to pay operating expenses while it sought rate relief in this proceeding. We will approve the use of the proceeds of the financing for this short-term loan given the unique nature of Eastman's present financial situation but ESC should take care in the future to seek rate relief on a more timely basis so that it does not place itself in the position of having to borrow money to pay general operating expenses. The rate impacts of this financing will be addressed in the permanent rate phase of this docket.

In conclusion, based upon our review of the filing and testimony and evidence presented at hearing, we find that the proposed financing is consistent with the public good and we will approve it. If the final terms and conditions of the financing vary materially from those

described above, such new or modified terms and conditions shall be subject to additional Commission approval.

Based upon the foregoing, it is hereby

ORDERED, that Eastman Sewer Company, Inc.'s request to borrow up to \$380,000 according to the terms described above is APPROVED; and it is

FURTHER ORDERED, that Eastman Sewer Company, Inc. shall file true copies of the loan documents executed or otherwise finally issued in connection with the closing of the transaction.

By order of the Public Utilities Commission of New Hampshire this twenty-first day of May, 2009.

Thomas B. Getz
Chairman

Graham J. Morrison
Commissioner

Clifton C. Below
Commissioner

Attested by:

Debra A. Howland
Executive Director