STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION

DG 09-239

NORTHERN UTILITIES, INC.

Petition for Approval to Issue Securities

Order Approving Petition and Setting Short-term Debt Limit

O R D E R N O. 25,068

January 22, 2010

APPEARANCES: Meabh Purcell, Esq., of Dewey & LeBoeuf LLP for Northern Utilities, Inc.; Rorie E.P. Hollenberg, Esq., for the Office of Consumer Advocate on behalf of residential ratepayers; Matthew J. Fossum, Esq., for the Staff of the Public Utilities Commision.

I. BACKGROUND

On November 24, 2009, Northern Utilities, Inc. (Northern or Company) filed a petition, pursuant to RSA chapter 369, for authority to issue securities. Northern is a regulated natural gas utility providing natural gas distribution service to various cities and towns in New Hampshire and Maine. By its initial petition, Northern sought authority to issue first mortgage bonds evidencing unsecured long-term debt in an aggregate amount of up to $20,000,000. On December 11, 2009, Northern informed the Commission that due to favorable market conditions, the amount of its debt issuance would be raised to $25,000,000. In support of its petition, Northern filed the pre-filed testimony and schedules of David Chong, Director of Finance for Unitil Service Corporation, which provides various professional and administrative services to Northern. In addition to the above financing, Northern will receive a $7,500,000 equity contribution from its parent, Unitil Corporation (Unitil), to support its capital structure, up from $5,000,000 as stated in the initial petition. Another subsidiary of Unitil, Unitil Energy Systems, Inc., has sought approval for financing concurrent with the instant petition on substantially similar terms. *See* Docket No. DE 09-236. In total, Northern would have approximately $32,500,000 in available funds following the issuance of the bonds and receipt of the equity contribution.

The bonds are to be sold at par by private placement to institutional investors. According to the petition, the targeted term of the notes issued by Northern is 10 years, and the notes are to bear an interest rate not to exceed 7.8 percent. By supplemental testimony of Mr. Chong dated December 21, 2009, Northern noted that it had completed an auction of the notes and had established a coupon rate of 5.29 percent for the notes.

The primary purpose of the financing is to refinance Northern's short-term debt by paying off approximately $32,090,000 in accrued debt. Northern notes that some of the short-term debt to be refinanced was incurred in conjunction with Unitil's purchase of Northern in 2008. Most of the remaining short-term debt was incurred in the completion of various capital projects since Northern's acquisition, including the extension of mains, installations of meters and services, and other improvements to its existing distribution system. Of the approximately $20,000,000 in capital projects completed, about $7,300,000 worth have been in New Hampshire, while the remainder were completed in Maine. Concurrent with this petition, Northern filed an essentially identical petition in Maine. *See* Maine Public Utilities Commision Docket No. 2009-391. On December 16, 2009 Maine regulators approved that petition.

Of the funds from this financing not going to the repayment of short-term debt, most are to pay the costs and expenses of the financing which are anticipated to total approximately $410,000. Northern proposes that these costs be incorporated as a portion of the costs of the financing and amortized over the life of the bonds. Any funds not consumed by the repayment of short-term debt or in covering the costs and expenses of issuance are to be used for "general corporate purposes." Northern's analyses indicate that any such funds would be minimal.

Northern's petition noted that the proposed financing and accompanying equity contribution will result in a stronger total debt to capitalization ratio for the Company and will allow the Company to retire outstanding short-term debt. Moreover, Northern stated that because the financial information in the petition was based on the Company's position as of September 30, 2009, and because natural gas distribution companies generally have stronger financial performances in the winter months, its ratio will improve further. According to the analysis submitted with its December 11, 2009 letter, Northern estimates that the financing and equity contribution will result in a pro forma capital structure, including short-term debt, of 41 percent equity and 59 percent debt compared to a capital structure of 37 percent equity and 63 percent debt absent the financing and equity contribution.

In addition to requesting approval of its issuance, Northern's petition also raised issues relating to the amount of short-term debt that it carried. At the time of the petition, Northern's ratio of short-term debt to net utility plant was higher than that generally considered acceptable to the Commission. Accordingly, by supplemental testimony Northern proposed a method for calculating an appropriate level of short-term debt going forward.

On December 11, 2009, the Office of Consumer Advocate (OCA) submitted a letter to the Commission expressing various concerns about Northern's request. Specifically, OCA raised concerns relative to the proposed interest rate and proposed costs of the financing, the proposed uses of the funds, the impact of the financing on customers, and the approval process sought by Northern. On December 17, 2009, the Commission issued an order of notice setting a hearing in this matter for January 5, 2010. On December 21, 2009, Northern submitted the supplemental testimony of Mr. Chong which updated some of the information from the original petition, and provided the Company's response to the concerns raised by OCA's letter.

On December 24, 2009, OCA submitted a letter, pursuant to RSA 363:28, II, indicating that it would participate "for the purpose of monitoring" the financing. On December 31, 2009, representatives of the Company, OCA and Staff met in a technical session, and a hearing was held on January 5, 2010 as scheduled.

II. POSITIONS OF THE PARTIES AND STAFF

A. Northern

Since the filing of the petition Northern has completed the private placement auction for its bonds and achieved an interest rate of 5.29 percent. After factoring in the issuance costs, the total cost rate for the new senior unsecured notes of $25,000,000 is 5.54 percent. Transcript of January 5, 2010 Hearing (Tr.) at 18. This "all-in" rate is still below the requested maximum rate of 7.8 percent. Hearing Exhibit 3 (Ex. 3), Supplemental Pre-Filed Testimony of David Chong at 2. According to Northern, it has locked in this rate and the rate fits within the range of rates for comparable utility market transactions. Ex. 3 at 2. Mr. Chong noted that Northern was "very pleased" with the results of the auction. Ex. 3 at 2; Tr. at 28. Additionally, Northern points out that any concerns OCA may have had about the amount of the interest rate have been addressed since the locked-in rate is well below that noted in the initial petition. Ex. 3 at 5.

As to the costs of the financing, Northern provided a breakdown of the various costs incurred in the financing, which total about $410,000. Ex. 3 at 6. Some of the costs, such as the placement fee which accounts for nearly half of the estimated costs, are outside the control of

Northern and thus would not be changed by use of a request for proposals (RFP) or similar process. Ex. 3 at 6; Tr. at 16. As to the costs within its control, Northern noted that the estimated fees for its attorneys, approximately, $150,000, are appropriate. Ex. 3 at 6-7. Though it did not use an RFP or other competitive process, Northern contends that hiring its attorneys was appropriate because of “the firm’s significant experience with utility financings, high quality of legal representation and its familiarity with Unitil and Northern.” Ex. 3 at 7. Significantly, Northern notes that its attorneys had acted as corporate counsel for Northern for nearly 30 years until about 2000 and thus have meaningful experience with Northern. Ex. 3 at 6. Northern is also responsible for the legal fees of the lender’s counsel, over which it has no control. Ex. 3 at 6. According to Northern, it is interested in controlling legal fees to the degree possible because they are amortized over the life of the financing, in this case 10 years. Ex. 3 at 8. As noted by Northern, the result of this treatment means that any money it pays out to cover fees will not be recouped until after it files for a base rate case, and even then recovery is spread out over time. Ex. 3 at 8. At the hearing, Mr. Chong indicated that he believed the final legal fees would be below the estimated amounts. Tr. at 26.

Regarding the uses of the proceeds of the debt issuance other than for financing costs, the majority is going to the repayment of short-term debt. The Company points out that Northern carried about $8,400,000 in short-term debt at the time it was acquired by Unitil in 2008, much of which was related to the actual costs of the acquisition. Ex. 3 at 9; Tr. at 15, 23. From that point, Northern has spent approximately $20,600,000 on capital expenditures and is budgeted to spend another $19,000,000 in 2010. Ex. 3 at 9. With Mr. Chong’s supplemental testimony, Northern provided a list detailing the capital projects that have been undertaken with at least some short-term debt in New Hampshire and Maine. Ex. 3, Schedule 2 at 3-4. Many of the major costs identified by Northern relate to the provision or installation of meters, services and mains, including the replacement of outdated bare steel mains. Ex. 3, Schedule 2 at 3-4; Hearing Exhibit 4, Response to Staff Data Request 1-2.

According to Northern, its weighted average cost of capital will decrease as a result of this financing because the transaction will lower its overall cost of debt. Ex. 3 at 10. This decrease will not be immediately apparent to ratepayers since it will not be reflected in rates until Northern's next base rate case, but, Northern contends, lowering the cost of debt will result in lower rates in the long-term. Ex. 3 at 10; Tr. at 16-17. As such, Northern contends that this transaction will improve its debt to equity ratio as well as result in lower long term rates for its customers. Ex. 3 at 10.

Also, in response to OCA's concern that the *nisi* order requested by Northern was not an appropriate manner in which to address a request for financing approval, Northern states that such a concern is mooted by the Commission holding a noticed hearing on the matter. Ex. 3 at 11. Thus, Northern states that there will be a public opportunity to explore the impact of the proposed financing and the issues potentially raised by the *nisi* process are no longer present. Ex. 3 at 11.

Finally, with regard to its short-term debt, Northern noted that at the time of its petition it carried approximately $33,200,000 in short-term debt and approximately $148,000,000 in net utility plant, giving it a ratio of short-term debt to fixed plant of 22.4% which is in excess of what is generally considered acceptable. Hearing Exhibit 1, Pre-Filed Testimony of David Chong, Exhibit NU-4. Pending issuance of its securities Northern proposes an interim short-term debt limit of $60,000,000, representing 35 percent of net utility plant. Hearing Exhibit 6, Response to Staff Data Request 2-3; Tr. at 13. The interim period would end upon the issuance of the long-term securities at issue here. Hearing Exhibit 6, Response to Staff Data Request 2-3.

Following the interim period, Northern proposed that its short-term debt limit be set with fuel-related and non-fuel-related factors. Under its proposal, Northern's short-term debt limit for fuel financing purposes would be set at 30 percent of its total projected winter period gas costs and would be set yearly with its winter cost of gas filing. Ex. 3 at 3. For purposes other than fuel financing, Northern initially proposed that its short-term debt limit be set at 10 percent of net utility plant and that it would be adjusted monthly. Ex. 3 at 3-4. Finally, Northern proposed, consistent with *Northern Utilities, Inc.*, Order No. 24,095 (December 13, 2002), that fuel inventory financing not be considered short-term debt and that a limit not be set on the amount of fuel inventory financed through the Unitil Cash Pool. Ex. 3 at 4. Northern later revised its proposal to set the non-fuel financing debt limit at 15 percent of net utility plant to accommodate environmental remediation and accelerated pipe replacement costs. Hearing Exhibit 7, Response to December 31, 2009 Oral Data Request. Additionally, Northern removed its proposal to exclude fuel inventory financing conducted through the Unitil Cash Pool. Hearing Exhibit 7, Response to December 31, 2009 Oral Data Request.

B. OCA

OCA's letter of December 11, 2009 expressed various concerns about Northern's petition as it was originally filed. As noted above, OCA was initially concerned that the interest rate proposed by Northern was excessive in that it seemed higher than the rates proposed in other long-term financing petitions filed by other companies in 2009. OCA also questioned the appropriateness of various factors used by Northern in establishing the proposed rate.

OCA expressed concerns about the costs of the financing, particularly the amount of estimated attorneys' fees. OCA contended that Northern had not provided any information in its filing to support a determination that the costs were objectively reasonable. Moreover, OCA contended that Northern's filing was silent on the manner in which it hired its outside counsel and about how the rates or fee estimates for its attorneys were determined.

OCA also questioned the adequacy of detail provided with regard to uses of the short-term debt that was to be refinanced, as well as the uses of any funds not going to the repayment of short-term debt or financing costs. Regarding the funds intended for the repayment of short-term debt, OCA contended that more information was needed about the uses of that money before a determination could be made about whether the proposed long-term financing was consistent with the public good. OCA contended that Northern's filing also lacked detail about the impact of this financing on Northern's customers.

Finally, OCA expressed concern about Northern's request for an order *nisi*. According to OCA, Northern's customers are entitled to notice regarding the Company's request, the proposed uses of the funds and the impact of the financing on customers' rates. OCA contended that an order *nisi* would not provide such notice. At the hearing, OCA did not question Mr. Chong or make a closing statement.

C. Staff

Staff did not testify at the hearing. In questioning Mr. Chong, Staff asked about the auction process for the bonds. Tr. at 19. Mr. Chong responded that the Company's placement agents had included six existing, and six new investors in the process and Mr. Chong believed that the process was a competitive one. Tr. at 19-20. Staff also inquired whether, given the favorable rate, it would make sense for Northern to refinance other portions of its existing debt. Tr. at 18. Mr. Chong responded that because of the “make whole” provisions governing its existing debt, it would have to obtain an interest rate far more favorable than was obtained here to make refinancing cost effective. Tr. at 18-19.

With regard to the Company’s short-term debt, Staff asked the Company to explain why establishing the limit was in the public interest. Tr. at 20. Mr. Chong responded that normal Company practice is to undertake capital projects with internally-generated funds and to supplement those funds as needed with short-term debt. Tr. at 20. Also, Mr. Chong noted that the limit would actively influence the Company to manage its capital structure appropriately and to access capital markets at appropriate times and within appropriate boundaries. Tr. at 20.

In its closing, Staff noted that the interest rate obtained by the Company was a favorable one and below the rates of the Company’s existing debt. Tr. at 25. Regarding the uses of the proceeds, Staff noted that the majority would be used to repay short-term debt that was spent on various capital projects. Tr. at 25-26. Staff noted that Northern had provided lists of the projects it completed using short-term debt and that the projects appear to be of the type done in the normal course of utility operations. Tr. at 25. Specifically, Staff noted that Northern had used the money to finance projects such as the installation of meters, mains and services. Tr. at 25-26.

Regarding the costs of the financing, Staff agreed that many of the costs are outside the Company’s control and therefore not subject to dispute. Tr. at 26. Staff stated that it found reasonable the Company's explanation that hiring its legal counsel without the use of an RFP or similar process was appropriate. Tr. at 26.

With regard to the Company's short-term debt limit, Staff did not oppose the Company's request for an interim limit of $60,000,000 since that limit would only stand until the bonds were issued around March 1, 2010. Tr. at 26. Regarding the limit of 30 percent for fuel financing purposes, Staff supported the limit. Tr. at 26-27. Staff noted that a similar approach is used by EnergyNorth and that it did not oppose using the same standard for Northern. Tr. at 26-27. Staff also noted that this amount could be adjusted annually when Northern filed its winter cost of gas. Tr. at 27. As to the 15 percent of net plant limit for non-fuel purposes, according to Staff the Company has stated that such a limit would be sufficient for at least a few years. Tr. at 27. Staff stated that the 15 percent limit was proper and served the goals of helping the utility meet its needs while protecting the Company's capital structure and long-term financial health. Tr. at 27. Staff stated that overall, it believed the financing request was in the public good and would help the Company control rates. Tr. at 27. Therefore, Staff supported the Company's request. Tr. at 27.

III. COMMISSION ANALYSIS

RSA 369:1 provides, in relevant part, that the Commission may approve the issuance and sale of securities "where it finds that the same is consistent with the public good." Moreover, "after such hearing or investigation as it may deem proper,"[1] the Commission will authorize the issuance of securities upon terms found to be consistent with the public good. RSA 369:4. In determining the public good, the Commission is to consider the amount of the issuance

[1] The Company requested an order *nisi* in this docket, but it was determined that the circumstances were sufficiently complex that a hearing was appropriate.

authorized, the purpose or purposes to which the proceeds are to be applied, and the reasonableness of the terms and conditions of the financing. RSA 369:1, :4. Additionally, a securities issuance entails consideration of whether the object of the financing is reasonably required for use in discharging a utility company's obligation to provide safe and reliable service, whether the plans to accomplish that object are economically justified when measured against any adequate alternatives, and whether the resulting capitalization would be supportable. *Appeal of Easton*, 125 N.H. 205, 211-213 (1984).

We recently stated that the review outlined by *Easton* requires looking "beyond merely the terms of the financing . . . ." *Public Service Company of New Hampshire*, Order No. 25,050 (Dec. 8, 2009). However, the review need not be the same in all instances, and some financing requests are more "routine" than others. *Id*. at 12. For example, a "routine" financing may be one "that will have no discernable impact on rates or deleterious effect on capitalization, [and] in which the funds are to enable numerous investments appropriate in the ordinary course of utility operations." *Id*. We concluded that "[t]he lesson of *Easton* is that certain financing related circumstances are routine, calling for more limited Commission review of the purposes and impacts of the financing, while other requests may be at the opposite end of the spectrum, calling for vastly greater exploration of the intended uses and impacts of the proposed financing." *Id*. at 14.

For the reasons discussed below, we conclude that the instant financing is "routine," and, as such, the manner of our review is tailored to the circumstances. We find such treatment appropriate because the amount of the financing is not excessive, and will not have a deleterious effect on capitalization. Moreover, the majority of the funds will be used to fund numerous investments of the type normally made in the ordinary course of utility operations. With this understanding, we turn to the specific issues presented by Northern's proposed financing.

Northern has marketed its bonds to investors through a private auction described by Mr. Chong and received a rate of 5.29 percent. The auction described by Mr. Chong appears to be a reasonable method that involves competitive market forces. Moreover, the interest rate obtained through this process is favorable in that it is well below the maximum rate initially requested by the Company as well as below the rates of the Company's other outstanding debt. As such, we find that the terms and conditions of the financing are reasonable.

As to the proceeds to be received from the final sale and issuance of the bonds, the Company proposes to use the majority for the repayment of short-term debt. Northern's initial filing did not explain the generation of the short-term debt sufficiently, but the Company subsequently addressed that shortcoming. The Company noted that at the time Unitil acquired Northern, Northern already carried approximately $8,400,000 in short-term debt. In reference to this debt in particular, Northern described it as being related "largely" to the financing of the acquisition as well as including some historical capital expenditures completed under Northern's prior corporate parent.

Since the acquisition, Northern has spent about $20,000,000 on capital projects, with about $7,000,000 spent in New Hampshire. Northern has provided detailed lists of the types of projects completed with these funds and the amounts that they cost. For example, Northern notes that it spent approximately $3,000,000 on the replacement of about four miles of bare steel mains, as well as about $500,000 on labor and materials for the installation of meters and piping for customers, which are the kinds of expenditures usually made in the normal course of utility operations. We note that we do not make a finding that the decisions to invest in these projects were prudent or that the costs for them were prudently incurred. We find only that they are of the type generally undertaken by utilities, such as Northern, in order to discharge their duty to provide safe and reliable service and to ensure the continuing viability of their distribution systems. Accordingly, with this understanding of the source of the short-term debt, we conclude that the repayment of short-term debt is in the public good. Moreover, given the routine nature of the projects giving rise to the short-term debt to be repaid, we find the use of the proceeds of this financing to repay that debt to be in the public good without further review of possible alternatives of the financing. *See Public Service Company of New Hampshire*, Order No. 25,050 at 16.

As to the costs of the financing, as both Northern and Staff pointed out, many of the costs are beyond the control of Northern, yet are necessary to complete a transaction such as this. Regarding the costs within its control – specifically its attorneys' fees – Northern noted that it did not use an RFP or similar process because it decided the best course was to use a firm familiar with its business and with the business of corporate debt issuances. Moreover, Northern noted that because it will not immediately recover amounts spent on its attorneys, it has an incentive to keep costs low. We find these explanations reasonable and likewise find that the costs of the financing are reasonable. The financing will also reduce Northern's overall cost of debt, improving its profitability and ultimately benefiting ratepayers. For the above reasons, we find that the financing as proposed by Northern is in the public good.

Regarding Northern's short-term debt limit, Northern has requested that it be set at $60,000,000 on an interim basis until the financing is completed on or around March 1, 2010.

While this limit is high compared to the Company's net plant, we nevertheless approve the amount since it will be in effect for only a short time.

Going forward, Northern has proposed, and Staff has supported, a short-term debt limit composed of a fuel factor and a non-fuel factor. The factor relating to the Company's fuel financing would be equal to 30 percent of the Company's total gas costs. We note that this amount is the same as that to which EnergyNorth is subject. *See EnergyNorth Natural Gas, Inc. d/b/a KeySpan Energy Delivery New England*, Order No. 24,824 (Feb. 29, 2008) at 3, 12-13. Also, as with EnergyNorth, the fuel factor of the short-term debt limit will not exclude Northern's fuel inventory financing requirements. Additionally, this amount will be set yearly in concert with the Company's cost of gas filing and may be reviewed and, if necessary, modified at that time. We find this to be a reasonable means of aiding the Company in controlling its costs while also allowing oversight of its spending practices.

The non-fuel factor is proposed to be set at 15 percent of net utility plant. Northern has indicated that this limit will be sufficient to allow it to conduct its normal operations as well as allow it to address environmental remediation costs and accelerated bare steel pipe replacement costs. We find this amount to be reasonable.

Based upon the foregoing, it is hereby

ORDERED, that the petition by Northern Utilities, Inc. to issue up to $25,000,000 in long-term debt, coincident with an equity contribution of $7,500,000 from Unitil Corporation, is hereby APPROVED; and it is

FURTHER ORDERED, that an interim short-term debt limit for Northern Utilities, Inc., in the amount of $60,000,000, is hereby APPROVED and shall expire upon the issuance of the aforementioned long-term debt or March 8, 2010 whichever is earlier; and it is

FURTHER ORDERED, that upon the expiration of the interim short-term debt limit, the short-term debt limit for Northern Utilities, Inc., shall, for fuel financing purposes, be 30 percent of total projected winter period gas costs, subject to adjustment annually with the Company's winter cost of gas filing, and it shall, for non-fuel financing purposes, be 15 percent of net utility plant.

By order of the Public Utilities Commission of New Hampshire this twenty-second day of January, 2010.

Thomas B. Getz Chairman	Clifton C. Below Commissioner	Amy L. Ignatius Commissioner

Attested by:

Debra A. Howland
Executive Director