

**STATE OF NEW HAMPSHIRE  
BEFORE THE  
PUBLIC UTILITIES COMMISSION**

**Re: Pennichuck East Utility, Inc. – Maple Hills/SRF Financing**

**DW 08-**

**DIRECT PREFILED TESTIMONY OF WILLIAM D. PATTERSON**

February 15, 2008

1 Q. Please state your name and business address.

2 A. My name is William D. Patterson. My business address is 25 Manchester Street,  
3 Merrimack, New Hampshire.

4 Q. By whom are you employed and what position do you hold?

5 A. I am employed by Pennichuck Water Works, Inc. ("PWW"), sister company of  
6 Pennichuck East Utility, Inc. ("PEU"). I serve as Senior Vice President, Treasurer and  
7 Chief Financial Officer of Pennichuck Corporation ("Pennichuck"), the parent company  
8 of both PEU and PWW.

9 Q. Have you previously testified before this Commission or in any other proceeding?

10 A. I have given live testimony and/or submitted written testimony in the following dockets  
11 before the New Hampshire Public Utilities Commission:

12 Rate Cases

13 Pennichuck Water Works, Inc.: DW 04-056

14 Pennichuck East Utility, Inc.: DW 05-072

15 Pennichuck Water Works, Inc.: DW 06-073

16 Pennichuck East Utility, Inc.: DW 07-032

17 Financing Cases

18 Pennichuck East Utility, Inc.: DW 05-061

19 Pennichuck Water Works, Inc.: DW 05-094

20 Pennichuck Water Works, Inc.: DW-05-152

21 Pittsfield Aqueduct Company, Inc.: DW 06-024

22 Pittsfield Aqueduct Company, Inc.: DW 06-030

23 Pennichuck East Utility, Inc.: DW 04-138

Pennichuck Water Works, Inc.: DW 05-152

Pittsfield Aqueduct Company: DW 07-010

Pittsfield Aqueduct Company: DW 07-120

I have also submitted written testimony or given live testimony previously in other  
5 forums in numerous matters.

6 Q. Please provide the Commission with an explanation of the purpose of the financing  
7 proposed by PEU in its petition in this proceeding (the “Proposed Financing”).

8 A. The purpose of the Proposed Financing is to fund a portion of the cost of certain capital  
9 improvements to PEU’s Maple Hills water system. The testimony of Donald Ware  
10 included with the Company's filing in this case will provide additional detail regarding  
11 the scope of what the proposed project encompasses.

12 Q. Please describe the overall financing plan for the capital improvements.

13 A. The estimated cost of the improvements is \$593,985. Substantially all the funding is  
14 anticipated to be provided by the proceeds of the Proposed Financing. In the event that  
15 the loan amount authorized by DES is not sufficient to fund completely the cost of  
16 improvements, the balance, if any, is anticipated to come from a mix of PEU’s internal  
17 cash flow from operations and/or inter-company advances from PEU’s parent company.  
18 The borrowing for which PEU is seeking approval in this docket is for up to \$595,000 to  
19 be provided from the State of New Hampshire Drinking Water State Revolving Loan  
20 Fund (“SRF”). As the Commission is aware, SRF funds are loaned by the State on  
21 extremely favorable terms. The low cost funds from the SRF will lower the overall cost  
22 of the financing needed to complete the capital improvements to the Maple Hills system.  
23 The State Department of Environmental Services (“DES”), which administers the SRF,

1 has included the Maple Hills project on the State's fiscal year 2007 Drinking Water State  
2 Revolving Loan Priority List, a copy of which is attached as Schedule WDP-1.

3 Q. What are the terms of the proposed SRF financing?

4 A. As the Commission is aware, the SRF provides public and private water systems the  
5 opportunity to borrow funds at below-market interest rates to fund the construction of  
6 qualified projects. The terms of the SRF loans are expected to require repayment over a  
7 twenty-year period, with interest at an expected rate not to exceed 3.488%. Six months  
8 after the project is substantially complete, monthly payments will consist of principal  
9 payments of approximately \$2,475 representing 1/240<sup>th</sup> of the total amount borrowed,  
10 plus interest. Amounts advanced to PEU during construction will accrue interest at a rate  
11 of 1%, and the total accrued interest will be due upon substantial completion of the  
12 project. Copies of the loan documents will be submitted to the Commission once they  
13 have been finalized and executed.

14 Q. What are the estimated issuance costs for these loans?

15 A. The anticipated issuance costs total \$7,500, and relate primarily to legal costs which will  
16 be incurred to (i) review and revise the necessary loan documentation prepared by the  
17 State and (ii) obtain Commission approval of the loans. The issuance costs will be  
18 amortized over the twenty-year life of the SRF loans. The annual amortization expense  
19 of approximately \$375 associated with the issuance costs has not been considered in  
20 Schedules WDP-2 through 4 due to its immateriality with respect to the overall analysis  
21 and impact of this proposed financing.

22 Q. Please explain Schedule WDP-2, entitled "Actual and Pro Forma Balance Sheet at  
23 December 31, 2007".

1 A. Schedule WDP-2 presents the actual financial position of PEU as of December 31, 2007  
2 and the pro forma financial position reflecting certain adjustments pertaining to the  
3 Proposed Financing.

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

5 A. Schedule WDP-2 contains two pro forma adjustments. The first adjustment for \$593,985  
reflects the increase in PEU's Plant in Service for the construction project and the related  
funding sources. The second adjustment reflects the after-tax effect on retained earnings  
for the annual interest expense accrued during the first year, with a corresponding credit  
to accrued expenses payable.

10 Q. Mr. Patterson, please explain Schedule WDP-3 entitled "Actual and Pro Forma Income  
Statement for the Twelve Months Ended December 31, 2007".

12 A. Schedule WDP-3 presents the pro forma impact of this financing on PEU's income  
13 statement for the twelve month period ended December 31, 2007.

14 Q. Please explain the pro forma adjustments on Schedule WDP-3.

15 A. Schedule WDP-3 contains two adjustments. Adjustment one is to record the estimated  
first year's interest cost related to the new funding sources. The second adjustment is to  
record the after-tax effect of the additional pro forma interest expense using an effective  
combined federal and state income tax rate of 39.6%.

19 Q. Please explain Schedule WDP-4 entitled "Actual and Pro Forma Statement of  
20 Capitalization at December 31, 2007."

21 A. Schedule WDP-4 illustrates PEU's actual total capitalization, as of December 31, 2007,  
22 which is comprised of common equity, funded debt and net inter-company advances.

23 Q. Please explain the pro forma adjustments on Schedule WDP-4.

1 A. Schedule WDP-4 contains two adjustments. The first pro forma adjustment reflects the  
2 after-tax decrease to retained earnings for the additional pro forma interest expense  
3 related to the new funding sources, while the second adjustment reflects the funding  
4 sources for the project.

5 Q. Mr. Patterson, are there any covenants or restrictions contained in PEU's other bond and  
6 note agreements which would be impacted by the issuance of debt under this proposed  
7 financing?

8 A. Yes. PEU's existing agreements contain three covenants governing the issuance of new  
9 PEU debt. These covenants specify minimum interest coverage ratios and maximum  
10 amounts of debt in relation to net plant and to total capitalization. PEU's actual ratios,  
11 pro formed for the SRF loans contemplated herein, are comfortably within these  
12 covenants.

13 Q. Has PEU's Board of Directors formally voted to authorize the Proposed Financing?

14 A. Not at this time. Resolutions authorizing the subject financing are scheduled for the next  
15 board meeting, which is anticipated to be held on March 13, 2008. Evidence of these  
16 resolutions will be provided promptly thereafter.

17 Q. Do you believe that the Proposed Financing is in the public interest?

18 A. Yes, I do. The projects being financed will enable PEU to provide safe, adequate and  
19 reliable water service to PEU's customers. For the reasons described in Schedule WDP-  
20 1, the capital improvements are needed in order to promote the public safety and welfare.  
21 The terms of the financing through the SRF are extremely favorable, and will result in  
22 lower financing costs than would be available through all other current debt financing

1 options including tax-exempt bonds issued through the New Hampshire Business Finance  
2 Authority.

3 Q. Is there anything else that you wish to add, Mr. Patterson?

4 A. Yes. I respectfully ask the Commission to issue an Order Nisi in this docket as soon as  
5 reasonably possible to enable PEU to begin the bidding and construction process for this  
6 project in the spring.

7 Q. Mr. Patterson, does this conclude your testimony?

8 A. Yes it does.

Pennichuck East Utility, Inc.  
DW 08-\_\_\_\_\_  
Schedule WDP-1

**DRINKING WATER STATE REVOLVING FUND  
FY 2007 PROJECT PRIORITY LIST**  
State of New Hampshire

1/2/2008

EPA#	TOWN	PUBLIC WATER SYSTEM	PROJECT DESCRIPTION	SYSTEM POPULATION	DISADVANTAGED COMMUNITY	PRIORITY POINTS	LOAN REQUESTED
0162130	Bartlett	Rolling Ridge	Interconnect with Bartlett Village Precinct	83	No	88	150,000
1973020	Raymond	Lamprey River Cooperative	Interconnect with Town of Raymond	45	Yes	78	100,000
0032010	Alexandria	Ledges at Newfound Lake	Install Disinfection, lead & copper treatment	160	No	78	157,000
1951010-15	Portsmouth	Portsmouth Water Department	Construction of new surface water treatment facility	33,000	No	68	22,000,000
0153060	Barrington	Emerald Acres Cooperative	Develop alternative water supply	250	No	64	117,500
1691010	New Hampton	New Hampton Village Precinct	Raw water transmission improvements	600	Yes	62	1,100,000
0512250	Conway	Saco Woods	Interconnect with Conway Village Fire District	240	Yes	62	825,000
0511010	Conway	Conway Village Fire District	Interconnect with North Conway, upgrade water mains	1,937	Yes	59	5,800,000
0841010	Franconia	Franconia Water Department	Install storage tank, upgrade distribution mains	750	Yes	55	3,400,000
0612020	Derry	Maple Hills	Interconnect with Town of Derry	458	No	53	520,000
1131010	Hill	Hill Water Works	Upgrade distribution mains, upgrade storage tank	350	Yes	53	825,000
1031010	Hampstead	Hampstead Area Water Company	Interconnect with Atkinson Water System	2,655	No	52	920,500
0142010	Barnstead	Locke Lake Water System	Upgrade distribution mains	1,710	Yes	49	250,000
1941010	Plymouth	Plymouth Water & Sewer	Construct new well and pump house	6,300	Yes	49	610,000
0511030	Conway	North Conway Village District	Develop new groundwater supply	5,000	Yes	42	2,410,000
1951010-09	Portsmouth	Portsmouth Water Works	Maplewood Avenue Main Replacement	33,000	No	42	3,000,000
1951010-10	Portsmouth	Portsmouth Water Works	Greenland well replacement and upgrade	33,000	No	42	2,000,000
1281020	Laconia	Laconia Correctional Facility	Upgrade distribution system	600	No	27	700,000
1951919-13	Portsmouth	Portsmouth Water Works	Water Source Augmentation	33,000	No	24	2,000,000

Total Need: 46,885,000

Denotes proposed projects which funding is available

Note: \$469,000 available from FY 06 Cap Grant  
\$1,023,000 available from Repayment Fund  
\$7,323,810 available from FY 07 Capitalization grant  
\$8,816,633 Total Available Project Funds



**Pennichuck East Utility, Inc.**  
**Actual and Pro Forma Balance Sheet as of December 31, 2007**  
**Unaudited**  
**Reflecting the Issuance of a \$593,895 SRF Loan**

<b>Assets</b>	<b>Actual Dec 31, 2007</b>	<b>Pro Forma Adjustments</b>	<b>Pro Forma Dec 31, 2007</b>
Plant in Service	\$ 27,780,713	\$ 593,985 <sup>1</sup>	\$ 28,374,698
Less: Accumulated Depreciation	(6,032,004)	-	(6,032,004)
Net Plant	<u>21,748,709</u>	<u>593,985</u>	<u>22,342,694</u>
CWIP	<u>242,713</u>	<u>-</u>	<u>242,713</u>
Total Net Utility Plant	21,991,422	593,985	22,585,407
Current Assets	690,641	-	690,641
Other Assets and Deferred Charges	<u>803,601</u>	<u>-</u>	<u>803,601</u>
<b>Total Assets</b>	<b><u>\$ 23,485,664</u></b>	<b><u>\$ 593,985</u></b>	<b><u>\$ 24,079,649</u></b>
Common Equity	\$ 6,046,759	\$ (12,514)	\$ 6,034,245
Current Portion of Long-term Debt	37,855	-	37,855
Other Current Liabilities	263,413	12,514	275,927
Long-Term Debt	6,469,136	593,985 <sup>1</sup>	7,063,121
Other Liabilities and Deferred Credits	<u>10,668,501</u>	<u>-</u>	<u>10,668,501</u>
<b>Total Equity and Liabilities</b>	<b><u>\$ 23,485,664</u></b>	<b><u>\$ 593,985</u></b>	<b><u>\$ 24,079,649</u></b>

**Notes:**

<sup>1</sup> To record the the issuance of a \$593,985 SRF loan to fund the Maple Hills Community Water System project

**Pennichuck East Utility, Inc.**  
**Actual and Pro Forma Income Statement for the Twelve Months Ended December 31, 2007**  
**Unaudited**  
**Reflecting the Issuance of a \$593,895 SRF Loan**

	<u><b>Actual</b></u> <u><b>Dec 31, 2007</b></u>	<u><b>Pro Forma</b></u> <u><b>Adjustments</b></u>	<u><b>Pro Forma</b></u> <u><b>Dec 31, 2007</b></u>
Operating Revenues	\$ 4,653,812	\$ -	\$ 4,653,812
O&M Expenses	2,845,604	-	2,845,604
Depreciation & amortization	425,284	-	425,284
Taxes other than income	328,937	-	328,937
Income taxes	249,952	(8,204) 2	241,748
Total O&M Expenses	<u>3,849,776</u>	<u>(8,204)</u>	<u>3,841,572</u>
Net Operating Income	<u>804,036</u>	<u>8,204</u>	<u>812,240</u>
AFUDC	<u>2,670</u>	<u>-</u>	<u>2,670</u>
Other Income (Expense)	<u>-</u>	<u>-</u>	<u>-</u>
Interest Expense:			
Funded debt	(363,929)	(20,718) 1	(384,647)
Inter-company debt	(61,703)	-	(61,703)
Total Interest Expense	<u>(425,632)</u>	<u>(20,718)</u>	<u>(446,350)</u>
Net Income	<u>\$ 381,074</u>	<u>\$ (12,514)</u>	<u>\$ 368,560</u>

**Notes:**

1 To record the annual interest (3.488%) on a \$593,985 SRF loan to fund the Maple Hills Community Water System project

2 To record income tax benefit (39.6%) resulting from additional interest

**Pennichuck East Utility, Inc.**  
**Actual and Pro Forma Statement of Capitalization as of December 31, 2007**  
**Unaudited**  
**Reflecting the Issuance of a \$593,895 SRF Loan**

	<u>Actual at Dec 31, 2007</u>		<u>Pro Forma Adjustments</u>		<u>Pro Forma at Dec 31, 2007</u>	
Common Equity:						
Common Stock	\$ 100		\$ -		\$ 100	
Paid in Capital	4,000,000		-		4,000,000	
Other Comprehensive Income	(56,926)				(56,926)	
Retained Earnings	2,103,585		(12,514)	1	2,091,071	
Total Common Equity	<u>6,046,759</u>	48.2%	<u>(12,514)</u>		<u>6,034,245</u>	45.9%
Debt:						
Current Portion of Long-term Debt	37,855		-		37,855	
Long-Term Debt	6,469,136		593,985	2	7,063,121	
Total Debt	<u>6,506,991</u>	51.8%	<u>593,985</u>		<u>7,100,976</u>	54.1%
 Total Capitalization	 <u>\$ 12,553,750</u>	 <u>100.0%</u>	 <u>\$ 581,471</u>		 <u>\$ 13,135,221</u>	 <u>100.0%</u>

**Notes:**

- 1 To record the annual interest (3.488%) on a \$593,985 SRF loan to fund the Maple Hills Community Water System project and  
To record income tax benefit (39.6%) resulting from additional interest
- 2 To record the the issuance of a \$593,895 SRF loan to fund the Maple Hills Community Water System project