STATE OF NEW HAMPSHIRE

PUBLIC UTILITIES COMMISSION

DG 15-155

In the Matter of:
Valley Green Natural Gas, LLC
Petition for Franchise Authority in Lebanon and Hanover

Direct Testimony

of

Stephen P. Frink
Assistant Director – Gas & Water Division

January 15, 2016

New Hampshire Public Utilities Commission

Valley Green Natural Gas, LLC

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Q. Please state your name, occupation and business address.

A. My name is Stephen P. Frink and I am employed by the New Hampshire Public Utilities Commission (Commission) as Assistant Director of the Gas & Water Division. My business address is 21 S. Fruit Street, Suite 10, Concord, New Hampshire 03301.

Q. Please summarize your educational and professional experience.

A. See ***Attachment SPF-1***.

Q. What is the purpose of your testimony in this proceeding?

A. The purpose of my testimony is to provide Staff's recommendations on whether Valley Green is in a position to provide natural gas utility service in Lebanon and Hanover at just and reasonable rates.

The testimony of Safety Division Staff witnesses provides Staff's recommendation on whether Valley Green has the managerial and engineering expertise to safely and reliably operate and maintain the proposed LNG facility and distribution system.

Q. Please summarize Staff's findings on these issues.

A. Staff recommends that the Commission not grant Valley Green's petition at this time and suspend the proceeding until Valley Green has a firm commitment from one or more anchor customer(s), as evidenced by signed contract(s) to be filed with the Commission.

Valley Green will not be able to provide service at just and reasonable rates without annual sales that can only be achieved by acquiring an anchor customer(s).

Q. Briefly describe the initial filing.

A. On May 15, 2015, Valley Green Natural Gas, LLC, of Hanover, New Hampshire (Valley Green) filed a petition to provide gas utility service in Lebanon and Hanover with the New Hampshire Public Utilities Commission (Commission). Valley Green intends to purchase liquefied natural gas (LNG) from domestic suppliers, store the LNG, process it through a regasification facility and distribute the natural gas through a pipeline distribution system to customers in Lebanon and Hanover. Valley Green will own the storage, regasification and distribution assets and offer both delivery service and a bundled (delivery and supply) service. The LNG storage and plant facilities will be located in Lebanon on a site leased from an affiliate company, Valley Green and Choice Storage. Valley Green will contract with Gulf Oil Limited Partnership (Gulf) for the operation and maintenance of the storage and regasification facility, and with TRI-Mont Engineering Co. (TRI-MONT) for the operation and maintenance of the pipeline distribution system. Gulf will be Valley Green's long-term supplier of LNG. Gulf is expected to sublease a portion of Valley Green's site on which Gulf will construct and operate an LNG vehicle fueling facility; Gulf is also expected to lease LNG tank space from Valley Green to support its vehicle fueling operations. New Energy Capital Partners, L.L.C. (NECP), a private equity firm, will be the primary equity investor in Valley Green and will finance all of Valley Green's development and construction costs. Following construction, NECP will solicit competitive debt providers to lower the cost of the capital. Valley Green expects to be profitable within the first year of operation.

Q. Has the Valley Green business plan changed since the initial filing?

A. Yes, Valley Green's business plan has changed as explained the Company's confidential response to Staff Data Request 3-2 dated January 8, 2016. The revised business plan does not address Staff's concerns regarding the financial feasibility of the project or Staff's recommendation that the Commission should not grant the petition at this time. Because the data response is confidential it is not attached to my testimony. Staff will request that the response be entered as a confidential exhibit at hearing.

Q. What are the requirements to own and operate a New Hampshire utility?

A. Any company seeking to own a utility must have the managerial, technical and financial expertise to operate it. Valley Green is in the process of acquiring that expertise.

Q. Does Valley Green have the managerial, technical and financial expertise to operate a natural gas utility?

A. Not at this time, Valley Green has never owned or operated a utility and does not currently have the systems and personnel in place to do so.

Q. Does Valley Green's lack of experience in operating a gas utility pose a risk?

A. Yes, although experience in not a prerequisite for operating a utility, not having operated a utility makes it more difficult to assess Valley Green's capabilities to do so. Experience can aid in: designing, locating and constructing facilities; developing operating plans and manuals; acquiring systems and staffing necessary for daily operations and emergency situations; ensuring a utility is aware of regional operating conditions and relevant regulatory requirements, such as reporting pertaining to public safety, customer service and finance; and, meeting its service obligations' cost effectively. Utility experience demonstrates operating capability, both positive and negative.

Q. How has Valley Green addressed the risks associated to its lack of experience?

A. The president of Valley Green, Mr. Campion, has worked with entities that have relevant experience related to the design, supply, operation and financing that are needed for natural gas utility operations and is in negotiations with vendors to provide those services on an ongoing basis.

Valley Green has used outside expertise with relevant experience in developing a business plan and preparing its filing. Valley Green has entered into a memorandum of understanding with Gulf Oil Limited Partnership (Gulf) under which Gulf will provide LNG to Valley Green and operate and maintain Valley Green's storage a regasification facilities. Valley Green hired TRI-MONT Engineering, Co. (TRI-MONT) to design its gas storage and regasification facility, and distribution system. Valley Green and TRI-MONT are negotiating a long-term contract whereby TRI-MONT will operate and maintain the Valley Green distribution system. A fund affiliated with New Energy Capital Partners, L.L.C. (NECP) will be the primary equity investor in Valley Green. NECP manages several funds on behalf of limited partners, whereby investors (primarily pension funds) commit capital to the fund and investments by the fund are made by the fund manager. NECP is currently managing over $300 million of affiliated funds and expects to have more than $100 million of new capital to invest in 2016.

For its rate analysis,Valley Green hired an individual that has experience in preparing and presenting rate proceedings before the Commission and its legal representatives have appeared before the Commission on behalf of other regulated utilities.

The Valley Green filing includes the direct testimony of TRI-MONT, Gulf and NECP witnesses stating their experience and explaining the services to be provided.

Mr. Campion has owned and operated a number of businesses in the proposed franchise area which should help in identifying and pursuing growth opportunities. Valley Green has identified the 10 largest potential customers in the proposed franchise, calculated their energy requirements and been in contact with each, all of which are located close to the proposed LNG facilities. The 10 largest customers, along with their load requirements and proximity to the LNG facilities, are identified in the Company's confidential response to Staff Data Request 3-1. Staff will request the response be entered as an exhibit at hearing.

Q. Are there other factors that mitigate the risks associated a lack of utility experience?

A. Yes, the franchise request is for a relatively limited area with little chance of economic expansion of utility service beyond Lebanon and Hanover. At full build out, given the limits of the franchise area and proximity of anchor customers, the entire distribution system is unlikely to exceed 20 miles and could be considerably less, and there will be a limited number of customers. Operating a small gas utility with all new facilities and a small customer base is far less risky than operating a large gas utility with aging infrastructure spread over a large geographical area and serving tens of thousands of customers.

Q. Is there sufficient demand to support natural gas utility service long-term?

A. That is very much in question. One potential customer, Dartmouth College, dwarfs all others and if a system is built to serve that load and Dartmouth College does not take service that could have an adverse impact on rate payers and/or shareholders. Even if the system is designed to serve only the potential non-Dartmouth College demand, fixed costs would be spread over lower sales and failure to sign anchor customers could cause financial stress. In either instance, Valley Green may not be able to offer reasonable rates, rates that would be competitive with alternative energy sources and provide a reasonable rate of return for shareholders.

Recently developments in the energy market are further exacerbating that risk, as there has been an extreme drop in oil and propane prices since Valley Green first formulated its business plan. Many of the potential anchor customers may have entered multi-year contracts to lock in lower prices and the energy savings, if any, from converting to natural gas may not justify the up-front costs of conversion.

Q. How do current oil and natural prices compare?

A. I heat my Manchester home with No. 2 fuel oil and received a delivery on December 28, 2015 priced at $1.92 per gallon. The equivalent delivered natural gas price is $1.53 per therm. The average residential heating customer per them rate for New Hampshire's two natural gas utilities are $1.46 and $1.40 based on rates in effect on November 1, 2015. See ***Attachment SPF-2.***

Q. How do current propane and natural prices compare?

A. A Staff employee recently received a propane delivery priced at $1.99 per gallon. The equivalent delivered natural gas price is $2.41 per therm. The average residential heating customer per them rate for New Hampshire's two natural gas utilities are $1.46 and $1.40 based on rates in effect on November 1, 2015. See ***Attachment SPF-2.***

Q. What are your expectations as to how Valley Green's utility rates will compare to current oil and gas prices?

A. Valley Green's utility rates will almost certainly be higher than those cited above and the oil and propane prices Commercial and Industrial (C&I) customers are currently paying are most likely lower than cited above. There will likely be little, if any, savings for C&I customers converting to natural gas utility service at this time.

As noted above, New Hampshire's natural gas utilities rates are only slightly above what residential oil customers are currently paying and Valley Green's rates are almost certain to be higher that the natural gas rates cited above. The supply portfolios of New Hampshire's natural gas utilities include natural gas delivered by pipeline to meet base load requirements and LNG to meet peaking requirements. Their supply portfolios are designed to meet total demand requirements at least cost. Valley Green does not have access interstate natural gas pipelines and will meet its demand requirements with LNG and/or CNG.

The oil and gas prices used in the above price comparison are those being offered residential heating customers in the Manchester and Concord area. C&I customers with significant usage should be able to negotiate much better prices and Lebanon and Hanover are only an hour north by truck.

Q. What other factors besides 'burner tip' price might potential customers take into account when considering natural gas utility service?

A. Other factors could include: lower emissions that could reduce air permitting fees; reduction in wear and tear on equipment from using a cleaner fuel, which could reduce maintenance costs and extend equipment life; pipeline delivery, thereby eliminating truck deliveries and on-site storage requirements; reliability, both as a base load supply and to back up renewables; and, reduced greenhouse gas emissions compared to other fossil fuels.

It is worth noting that the Dartmouth College energy working group's draft findings include getting off #6 fuel oil by 2016 as part of its efforts to reduce greenhouse gas emissions. See ***Attachment SPF-3***.

Q. Is there a 'demonstrated need' requirement for approval of a new utility?

A. Not per se. Unlike the Federal Energy Regulatory Commission, where approval of a new pipeline is highly contingent upon demonstrated market need as evidenced by long-term contracted customer commitments, there is no such requirement for New Hampshire utilities. That said, the ability to finance a utility is dependent on its ability to generate enough revenue to meet operating costs and achieve a reasonable rate of return. When considering petitions from each of the existing New Hampshire natural gas utilities for approval of their last major expansion into a new franchise area, there was a also a petition for approval of a special contract with an anchor customer to be served under a long-term contract with a take-or-pay requirement (a customer obligation to pay for certain volumes regardless of whether or not the customer uses those volumes). The special contracts demonstrated a need for the expansion and reduced the economic risk related to it.[1]

Q. What would be the consequences if Valley Green were to commence service and failed to achieve projected sales?

A. If Valley Green commences utility service and is unable to generate sufficient sales to sustain operations at a reasonable rate, the result could be economic failure, in which case Valley Green investors, employees, vendors and customers could experience economic harm.

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1 See Order Nos. 22,297 issued August 28, 1996 approving Northern Utilities, Inc. Petition for Approval of a Firm Gas Transportation Agreement and Expansion of Service and 22,667 issued July 22, 1997 approving EnergyNorth Natural Gas, Inc. Special Contract with Hitchiner Manufacturing Co, Inc.

Q. Given the financial uncertainty, why is NECP planning to invest in Valley Green?

A. The results of the NECP financial analysis indicates that the project will satisfy the internal rate of return its investors are seeking. NECP may be investing in both the regulated and unregulated businesses and the return on the unregulated business has greater certainty and a robust enough return that it is willing to accept a greater risk and lower return on its investment in the utility. NECP has an office in Hanover and invests in energy projects throughout the country so it may know more about the national and local market than is apparent in the filing. I assume NECP is monitoring the energy markets and customer commitments throughout the design phase and will not make a substantial investment until confident that the customer base will be sufficient to achieve the desired return. If NECP were to withhold funding, the project may be delayed or canceled.

Q. What analysis has been undertaken to determine if Valley Green's rates would be fair and reasonable?

A. Valley Green calculated a revenue requirement for the first and fifth years of operations using a revenue requirement template provide by Staff based on several scenarios. The scenarios and revenue calculations were provided in confidential responses to Staff Data Requests 3-8 and 1-2. The revenue requirement is based on expected rate base, revenue, expense and rate of return. The data responses also include the number of customers, billed sales and average per therm rate by customer class. Because the information is confidential and Staff's recommendations are not dependent on that information, the Company's data responses are not attached to my testimony. Staff will request the response be entered as a confidential exhibit at hearing.

Q. Are the assumptions used in the Valley Green's rate analysis reasonable?

A. The rate base, costs and capital structure appear reasonable to serve projected demand. Projected demand does not appear reasonable when considering the natural gas rates compared to current oil and propane prices. Converting C&I customers to natural gas at this time will be challenging, as large C&I customers may have multiyear contracts with current suppliers and the projected energy savings from converting may not satisfy the return on investment that would incent large C&I customers to convert.

Q. Can a customer contract for utility service with Valley Green prior to franchise approval?

A. Yes, there is nothing to prevent Valley Green from entering an agreement with potential customers, agreements would be subject to Commission approval of the franchise request, tariffs and, if the terms of service differed from the approved tariff, approval of the special contract.

Q. Do you believe Valley Green can sustain utility operations over the long-term?

A. Only if Valley Green is able to acquire sufficient load to enable it to recover fixed and variable costs at rates that are competitive with those of alternative energy providers and produce a reasonable rate of return for shareholders.

Q. What are the financial risks if the Commission were to approve the Valley Green petition at this time?

A. Valley Green may not achieve the sales necessary to support long-term operations. Capital and operating costs are largely dependent on serving a specific load, without a reasonable assurance targeted customers will take service the LNG facilities and distribution system may be over or under built which could impact rates and/or shareholder returns. To some extent customers are protected through the rate process, as cost recovery will be addressed in a future proceeding and Valley Green will carry the burden of proof in its rate filing that the investments were prudent and used and useful. Even with that protection, ratepayers could be harmed if Valley Green were denied recovery of a substantial portion of its investment from utility customers that resulted in a higher cost of capital.

There is also the risk that a rates and services to be provided by Valley Green may be less favorable that what Lebanon and Hanover ratepayers might see if the franchise were granted to another entity.

Q. Do you see any other risks in approving the petition?

A. Valley Green would hold exclusive rights to the franchise territory and could delay the provision of utility service indefinitely, denying potential customers the possibility of obtaining utility service at an earlier date, or at all, from a competing entity. Also, if Valley Green were to fail, what to do with the utility plant and distribution system would need to be addressed.

Q. Are there advantages in approving Valley Green's petition at this time?

A. Yes. Valley Green will have the legal authority to provide utility service which could make it easier to attain customer commitments. Potential customers may have more confidence in Valley Green's ability to provide utility service based on Commission approval, and customers desiring utility gas service will have no other option.

Q. Are there any other advantages in approving Valley Green's petition, either now or at a later date?

A. Yes. Prior to commencing service the financial risks are entirely Valley Green's. Organizational, design, marketing, permitting, regulatory, construction and other startup costs incurred by Valley Green will not be recovered from New Hampshire ratepayers until Valley Green files a rate case, receives Commission approval of tariffed rates and commences service. If Valley Green does commence service, the cost of service will be borne by its Lebanon and Hanover customers with no risk of cross subsidies from ratepayers outside of the franchise area.

Q. What kind of contract would demonstrate customer commitment?

A. A signed contract between Valley Green and a customer that requires a financial commitment from the customer, such as a deposit, contribution in aid of construction or a special contract with must take provisions. If it is a special contract, Valley Green would have to demonstrate that the terms of the contract cover Valley Green's marginal and embedded costs to serve the customer.

Q. What level of customer commitments does Staff recommend for Commission approval?

A. Expected margins from customer commitments should be sufficient to demonstrate the project is economically feasible. Given the limited price advantage, if any, of natural gas utility service with current oil and propane prices, customer commitments will need to be significant to demonstrate economic feasibility. How significant depends on the strength of the supporting business plan, a strong business plan that provides a reasonable assurance that the sales targets will be met reduces the level of customer commitments needed to demonstrate economic feasibility. In this instance, Staff recommends estimated margins from customer commitments meet or exceed fifty percent of the required margins necessary to achieve a ten year payback.

Q. Does that conclude your testimony?

A. Yes.