

HAMPTON WATER WORKS COMPANY

Petition for Approval of Affiliate Arrangement

Order Approving Financial Services Agreement and  
Increasing Short-Term Debt Limit

O R D E R    N O.    23,535

July 21, 2000

I.    **PROCEDURAL HISTORY**

On May 4, 2000, Hampton Water Works Company (Hampton or the Company), a New Hampshire corporation doing business as a public water utility in the Towns of Hampton, North Hampton and Rye, New Hampshire, and a subsidiary of American Water Works Company (AWW or Parent), filed<sup>1</sup> a Petition for approval of a Financial Services Agreement (Agreement) between Hampton and American Water Works Financing Corporation (AWCC<sup>2</sup>), also an AWW subsidiary. The stated purpose of the Agreement is to provide a mechanism for AWW and all its subsidiaries only to

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The filing was made pursuant to RSA 366:1, but should have been made pursuant to RSA 366:3 ten (10) days **after** the date the Agreement was entered into.

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On May 18, 2000, Hampton notified the Commission that the name of the corporation was changed to American Water Capital Corporation, hence the acronym AWCC is used throughout this Memorandum. AWCC is a Delaware corporation located in Vorhees, NJ, with its own Board and Officers. AWCC staffing will be drawn from personnel employed in the operating subsidiaries.

access short and long-term borrowings at advantageous terms, and to provide cash management through cash sweeps and investment of excess cash. Hampton is seeking approval, pursuant to RSA 366:5, of the affiliate arrangement, the Agreement and promissory notes attached thereto. AWW anticipates system-wide savings of \$400,000 to \$900,000 annually. The Petition also mentioned that Hampton's borrowings may, from time to time, with the Commission's approval, exceed 10% of the Company's net fixed capital.

The Testimony of Rod P. Nevirauskas, Hampton's Assistant Treasurer, in support of the Petition was filed on May 8, 2000. A copy of the unexecuted Agreement, along with Appendix 1 and Exhibits A & B, was filed on May 12, 2000.

On May 18, 2000, Commission Staff (Staff) submitted a list of 45 interrogatories and data requests, which were answered by the Company on May 25, 2000.

The Petition did not expressly request approval for borrowing in excess of 10% of net fixed capital, the maximum allowed by Puc 608.05, nor did it seek a waiver of the rule pursuant to Puc 201.05. However, after discussions with Staff, on June 1, 2000, Hampton filed a letter requesting such a waiver based upon the additional expected borrowing of approximately \$900,000 associated with the Lafayette Road (US

Rt. 1) main relocation project.<sup>3</sup> Hampton avers that borrowing requirements for the fiscal year beginning July 1, 2000 are expected to peak at \$2,500,000.

On June 27, 2000, Hampton filed an executed copy of the Agreement dated as of June 15, 2000.

## **II. BACKGROUND**

The Company's short-term borrowing requirements are currently established through an annual line of credit with Citizen's Bank of Boston. The current short-term line of credit of \$1,500,000 is established at 60 basis points over the federal funds rate. The Company also pays 35 basis points on the maximum authorized line of credit as a commitment fee. The proposed rate will be 15 basis points over the 30-day LIBOR rate with no commitment fee, but with a 10 basis point facility fee. Hampton expects to require short-term borrowing of \$1 - \$2.5 million over the next four years. Based on Hampton's stated net fixed capital of \$17,380,700, the maximum amount that could be borrowed short-term without Commission approval pursuant to Puc 608.05 would be 10% of that amount, or approximately \$1,700,000. AWCC will obtain funds to provide short-term loans to participants via a syndicated credit line.

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See Order No. 23,412 (Feb. 28, 2000) in Docket DW 99-057.

Hampton's long-term financing is usually obtained by private placement offerings on the open market. Hampton currently has three (3) outstanding issues of long-term debt totaling \$7.5 million with annual interest rates of between 7.48% and 9.92%, with expiration dates from 2019 through 2027. While neither Parent nor most of the subsidiaries are rated, the Company avers that AWCC's rating will be A or A-, similar to that of the three subsidiaries that are rated. The Company does not foresee any immediate long-term borrowing needs. The Company avers that it could borrow long-term at a rate 28.8 basis points lower through AWCC than it could otherwise and save on issuance costs as well. AWCC will make long-term loans available to participants from funds obtained by the sale of its own debt securities in the public market by filing a "shelf registration" with the SEC. Hampton will apply to the Commission for specific approval of any proposed long-term financing in excess of twelve months.

As part of the cash management services, subsidiary companies with excess cash will lend to other subsidiary companies through AWCC. Excess cash is swept down on a daily basis to pay down any outstanding lines of credit; if no amounts are outstanding, excess funds are invested overnight.

The interest rate charged for cash loaned to another participant will be the rate that AWCC is earning on the excess cash it has invested. Participants will not be required to do their borrowing through AWCC. Participants will not be responsible for the obligations of other participants as the obligations are several and not joint. On the other hand, AWW will issue a "support" letter for the benefit of purchasers of AWCC's debt. That letter will specifically exclude recourse to the regulated subsidiaries. Hampton and other participants may terminate the Agreement by giving ten (10) days written notice, while AWCC may terminate upon ninety (90) days prior written notice. Termination will not affect any amounts then outstanding.

Expenses of AWCC related to bank credit lines and short-term public borrowings, including initial start-up costs, will be allocated to the participants based upon their individual short-term borrowing requirements, i.e. the maximum line forecasted, as compared to total system borrowing requirements, excluding existing non-AWCC borrowings. Long-term borrowing costs will be passed through to each participant in proportion to the principal amount of that borrowing loaned to the participant. Overhead costs will be apportioned based upon each participant's long and maximum

short-term borrowings and investments. For the first 12 months beginning July 1, 2000, Hampton will be responsible for 2.5/643, or 0.4% of the total overhead cost. There will be no adjustment based upon actual borrowings.

AWCC will be required to make periodic reports to the Securities and Exchange Commission, and has agreed to file those reports with the Commission if requested to do so. The Company also agreed to report, on an annual basis, the results of participating in this Agreement.

The Agreement has been approved in at least two (2) other jurisdictions on behalf of Hampton affiliates. See Illinois Commerce Commission Order in Docket 00-0306, *Illinois-American Water Company*, May 16, 2000, and Connecticut Department of Utility Control Order in Docket No. 00-05-09, *Connecticut- American Water Company*, June 22, 2000.

### **III. COMMISSION ANALYSIS**

RSA 369 provides public utilities in New Hampshire with the authority to issue securities, subject to the approval of the Commission. Specifically, RSA 369:1 provides for the issuance of securities payable more than 12 months after their issuance, while RSA 369:7 provides for the issuance of short-term debt. Regarding short-term debt, the Commission has promulgated Puc 608.05 which limits such

indebtedness to 10% of a utility's net fixed plant, unless a waiver is requested and approved in accordance with Puc 201.05.

RSA 366 gives the Commission authority to investigate any affiliate arrangement, and, after notice and hearing, make a finding that the contract, arrangement, purchase or sale is unjust or unreasonable. RSA 366:5. The Commission may disapprove the same and disallow payments thereunder. In addition, even under existing contracts or arrangements the Commission has the authority to disallow charges unless the public utility shall establish the reasonableness of such payment or compensation. RSA 366:7. All such affiliate contracts must be filed with the Commission within 10 days **after** the date on which the contract is made. RSA 366:3.

The Commission has approved similar arrangements in the past. See *Re UNITIL Power Corporation*, 71 NHPUC 121 (1986); *Re UNITIL Power Corporation*, 71 NHPUC 567 (1986); *Re Kearsarge Telephone Company*, 74 NHPUC 45 (1989); and *Re Meriden Telephone Company*, 74 NHPUC 50 (1989).

Based on the filings, information provided to Staff and the Commission's experience with other utilities, it would appear that Hampton could realize savings from the proposed

arrangement, especially in view of Hampton's small size. The Agreement could allow Hampton to borrow at lower net rates while earning interest at a greater rate on any excess cash. For example, according to the Commission's Economics Department, the current Federal Funds Rate is 6.5% and the 30-day LIBOR rate is 6.6625%. Based on the information provided by the Company as noted above, this would result in a current interest rate of 7.1% vs. 6.9125% under the proposed plan. In addition, Hampton would save \$8,750 in commitment fees on a \$2.5 million line of credit. It is unknown at this time whether the overhead expenses will exceed those savings, however, given Hampton's 0.004% of overhead expenses, net savings is probable. Staff has, therefore, recommended that the Commission issue an Order authorizing Hampton to enter into the Agreement and increase its short-term borrowing limit to \$2.5 million, subject to the following conditions:

- a. The Commission's ongoing authority under RSA 366:7 to review the reasonableness of interest income, payments and allocations; and
- b. The Commission's authority to have access to AWCC's books, records, bills, accounts and other documents; and

- c. AWW providing to the Commission a copy of any and all "support letters" issued from time to time for the benefit of purchasers of AWCC's debt; and
- d. AWCC providing to the Commission copies of periodic reports to the Securities and Exchange Commission; and
- e. Hampton's reporting, on an annual basis along with its Annual Report to the Commission, the results of participating in this Agreement, including the amounts loaned to and/or borrowed from the AWCC, the costs of borrowing from the AWCC as opposed to what the costs would have been had the Company borrowed from a conventional lender, the net savings of all transactions with the AWCC as opposed to how the Company presently conducts its business and handles its own cash operations, and any other relevant information which would present a clear picture of the results of participating in this agreement; and
- f. Limiting such approval to short-term debt and cash management only; and
- g. Providing that Hampton seek specific approval for the issuance of securities other than short-term debt; and
- h. Hampton providing the Commission with copies of all orders in other jurisdictions, not already provided,

relating to this arrangement within ten (10) days of their issuance; and

- i. Hampton's submitting to the Commission any modification to the terms specified in the Agreement within ten (10) days after they are executed in accordance with RSA 366:3.

**Based upon the foregoing, it is hereby**

**ORDERED,** that Hampton may enter into the Agreement with AWCC, subject to the conditions noted above; and it is

**FURTHER ORDERED,** that Hampton's short-term indebtedness shall not exceed \$2,500,000.

By order of the Public Utilities Commission of New Hampshire this twenty-first day of July, 2000.

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Douglas L. Patch  
Chairman

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Susan S. Geiger  
Commissioner

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Nancy Brockway  
Commissioner

Attested by:

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Thomas B. Getz  
Executive Director and Secretary