

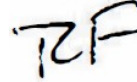
# STATE OF NEW HAMPSHIRE

## Inter-Department Communication

**DATE:** July 14, 2020

**AT (OFFICE):** NHPUC

**FROM:** Jay E. Dudley, Utilities Analyst IV



**SUBJECT:** DE 20-076 Unital Energy Systems, Inc. Petition for Authority to Issue Securities

**TO:** Commission  
Debra A. Howland, Executive Director  
Tom Frantz, Director Electric Division  
David Wiesner, Director Legal Division  
Mary Schwarzer, Staff Attorney

On May 20, 2020, Unital Energy Systems, Inc. (UES or the Company), filed a petition for authority to issue long-term debt not to exceed an aggregate principal amount of \$35 million. UES's filing comprised testimony and attachments including information provided by Form F-4 under N.H. Admin. Rule Puc 308:12. Staff recommends that the proposed financing be approved as submitted.

### *Description of Proposed Financing*

UES proposes to issue and sell up to \$35 million in aggregate principal amount long-term debt in the form of first mortgage bonds (the Bonds) during the period from the date of the Commission's order in this docket through December 31, 2020. The Company seeks authority to: (i) to refinance UES's existing short-term debt balance of \$25 million (as of March 31, 2020)<sup>1</sup>; (ii) to fund, in part, approximately \$9.5 million in planned capital expenditures for 2020; and (iii) to fund approximately \$500,000 in issuance costs.<sup>2</sup> As such, a portion of the request, approximately \$25 million, does not represent new indebtedness for UES since it constitutes the refinancing of existing debt, whereas the remainder of approximately \$9.5 million (after deducting approximately \$500,000 in estimated issuance costs) constitutes new debt. The maturity of the Bonds will range from 1 to 30 years. The Company proposes to price the Bonds at a fixed rate based on either the 10-year or 30-year U.S. Treasury rate plus a credit spread not to exceed two hundred eighty basis points (2.80%) resulting in a coupon rate of 3.41% to be determined at the time of closing.<sup>3</sup> UES anticipates that the ultimate rate for the Bonds

<sup>1</sup> Testimony of Todd R. Diggins at Bates 12.

<sup>2</sup> \$35 million minus (\$25 million plus \$500,000) = \$9.5 million. See Testimony of Todd R. Diggins at Bates 12 (\$25 million in short-term debt) and at Bates 11 (estimated costs of issuance approximately \$500,000).

<sup>3</sup> Based on 10-yr Treasury rate of 0.605% as of July 10, 2020. Treasury rates are subject to change daily.

will be consistent with current market rates; however, given that UES plans to close on the Bonds at some point within the third quarter (target date September 15, 2020) the Company requests approval of a maximum coupon rate of 5.25% in order to provide sufficient flexibility in the event of unanticipated widening of credit spreads due to uncertainty or volatility in the capital markets. The final financing structure, terms and conditions, amounts, documentation, and rate will be determined at the time of issuance.

The Company's filing includes the direct testimony of Mr. Todd R. Diggins, Treasurer and Director of Finance for Unitil Services Corporation (USC). USC provides various professional and administrative services to UES and Unitil Corporation's other utility subsidiaries. The filings' other attachments includes its Form F-4 including exhibits demonstrating the impact of the proposed financing on UES's balance sheet (CONFIDENTIAL Exhibit UES-4), income statement (CONFIDENTIAL Exhibit UES-5), capitalization (Exhibit UES-6), and cost of debt (Exhibit UES-7). UES estimated the cost of the bond issuance to be approximately \$500,000, which includes ratings fees, legal fees, and underwriting fees. The Company calculates, on a pro forma basis, that the new debt of approximately \$9.5 million, plus the refinance of the \$25 million in short-term debt, and approximately \$500,000 in issuance costs, will result in a small increase in annual interest expense.<sup>4</sup> However, despite the addition of new debt of approximately \$9.5 million, UES projects that after giving effect to the resulting pro forma adjustments, the proposed financing will not have a significant impact on the Company's current capital structure of 53% debt, resulting in a revised capitalization of 55% debt and 45% equity.<sup>5</sup> Commission Staff (Staff) confirmed UES's current bond ratings of BBB+ with Standard & Poor's, and Baa1 with Moody's Investors Service; these ratings also appear in UES testimony.<sup>6</sup> Both ratings agencies report an outlook of "Stable." The ratings agencies reports, including analyses and ratings, are also available in Data Response Staff 1-1, CONFIDENTIAL Attachments 1 and 2.

### ***COVID-19 Impacts***

In its filing, UES represents that the COVID-19 pandemic has not impacted the Company's decision to issue the Bonds given that UES's need for long-term debt financing is driven by capital spending which is continuing and ongoing. However, the Company's placement agent has recommended that UES act expeditiously due to recent increases in market issuances and a potentially volatile macroeconomic situation. Nevertheless, current bond market conditions remain conducive to new issuances, and the private placement market has been active and resilient, thus market conditions should result in advantageous rates for UES if it acts quickly.<sup>7</sup>

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<sup>4</sup> Those amounts can be found in CONFIDENTIAL Exhibit UES-5. UES did not provide a projected rate impact for the increase in interest expense, but represented that the increase would be included in the cost-of-service components to be filed by the Company in its next rate case.

<sup>5</sup> Testimony of Todd R. Diggins at Bates 17; Exhibit UES-6.

<sup>6</sup> *Id.* at Bates 16; <https://www.moodys.com/credit-ratings/Unitil-Energy-Systems-Inc-credit-rating-825615655> (Moody's public website where, with registration, Unitil Corporation's credit rating Baa1 is posted); [https://www.standardandpoors.com/en\\_US/web/guest/home](https://www.standardandpoors.com/en_US/web/guest/home) (S&P public website where, with registration, Unitil Corporation's credit rating BBB+ is posted).

<sup>7</sup> Testimony of Todd R. Diggins at Bates 13-14.

UES states that it will provide the Commission with an update of the final pricing parameters including the final coupon rate once the Bonds have been priced.<sup>8</sup> Staff supports this and recommends that the Commission require UES to file these updates along with an updated response to Data Response Staff 2-2, including attachment 1, the Bond Purchase Agreement, and Exhibit UES-7 (in both PDF and Excel), “the Weighted Average Cost of Debt,” following the final closing and funding, and no later than March 31, 2021.<sup>9</sup>

***Staff’s Recommendation***

Staff has reviewed the Company’s petition and supporting documents and believes that UES’s filing is complete and meets all requirements of Puc 308.12. Accordingly, it is Staff’s opinion that, based on the current total of outstanding long-term debt reported by UES,<sup>10</sup> the proposed refinance of existing debt in the amount of \$25 million, plus new debt of approximately \$9.5 million, will have a limited impact on UES’s capital structure, and the Company’s cost of debt and revenue requirement. As such, Staff supports the Company’s position that approval of the petition would be in the public good, and in conformance with the review standards of RSA Chapter 369. Therefore, Staff recommends that the Commission authorize UES to issue \$35 million in long-term debt, according to the proposed terms, amounts, and interest rate outlined above, for the purposes of refinancing and replacing a portion of its existing debt, and to include the issuance of new debt to fund planned capital expenditures for 2020.

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<sup>8</sup> *Id.* at Bates 17, 21.

<sup>9</sup> Data Response Staff 2-2 requested copies of the private placement memorandum including any purchase and sale agreement and letter of commitment from the lender. The Bond Purchase Agreement provided by Unitil was available in draft form only since the transaction for the Bonds is not yet finalized.

<sup>10</sup> *See* CONFIDENTIAL Exhibit UES-4.

Executive.Director@puc.nh.gov

amanda.noonan@puc.nh.gov

epler@unitil.com

jay.dudley@puc.nh.gov

Mary.Schwarzer@puc.nh.gov

ocalitigation@oca.nh.gov

richard.chagnon@puc.nh.gov

tom.frantz@puc.nh.gov