

STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION

IR 22-048

ELECTRIC, GAS, AND WATER UTILITIES

Investigation of Step Adjustment Methodology and Process

Statement and Submission into the Docket by Pennichuck Water Works, Inc., Pennichuck East Utility Inc. and Pittsburg Aqueduct Company, Inc.

My name is, Larry Goodhue, Chief Executive Officer and Chief Financial Officer of Pennichuck Water Works, Inc. (PWW), Pennichuck East Utility, Inc. (PEU), and Pittsburgh Aqueduct Company, Inc. (PAC), and I hold these roles for all the subsidiary corporations, and the parent Penn. Corp itself.

As indicated during the Pre-Conference Hearing for this docket on October 12, 2022, we are providing this written statement as a submission into the docket. Specifically, we feel it vitally important to make the Commission aware of our concerns as they pertain to the existing Step Increase mechanisms in place for our regulated companies, specifically the Qualified Capital Project Adjustment Charge (QCPAC) authorized for both Pennichuck Water Works, Inc. and Pennichuck East Utility, Inc. On September 26, 2016 (Order No. 26,070) the Commission approved the QCPAC mechanism (replacing the Water Infrastructure and Conservation Adjustment – WICA) for PWW. On October 4, 2018 (Order No. 26,179), the Commission approved a similar QCPAC mechanism for PEU.

As has been asserted and testified to in multiple dockets for our three regulated companies, and due to our unique ownership structure, which came out of the approved acquisition of Penn Corp by the City of Nashua in DW 11-026 on November 23, 2011 (Order No. 25,292). Cash flow coverage for our regulated utilities is paramount in order to adequately and fully cover debt service: (1) in addition to adequate cash flows to pay for the City Bond Fixed Revenue Requirement (CBFRR) component or our allowed revenues, for monies due the City to service the bonds issued to effectuate the acquisition, and (2) provide adequate cash flows to cover necessary and prudent operating expenses, in a rate structure devoid of any Return on Equity (ROE) or Return on Rate Base (ROR).

The purpose of the QCPAC was and is to establish a revenue requirement and associated customer rates sufficient to recover debt service and expenses associated with either PWW's or PEU's capital improvements (debt service x 1.1 plus incremental property taxes) on an annual basis, as layers of incremental debt-funded capital investments are made requiring the ability to service that incremental debt, rather than wait for recovery of such costs as part of a general rate case conducted every three years. The QCPAC mechanism acknowledges that PWW and PEU, are highly unique public utilities because they are ultimately owned entirely by the City of Nashua. Each Company must rely entirely on debt financing for its operations and capital expenditures. The QCPAC was not requested for implementation at this time for PAC, as its only

sources of external debt funding currently are SRF or DWGTF loans or grants. The nature and magnitude of those borrowings are sporadic in their issuance or overall value, and as such, can currently be addressed as an element of rates for PAC in its periodically filed rate cases.

In contrast to PWW and PEU, other traditional investor-owned utilities have significant equity owners, and this equity position allows those utilities to carry the additional direct financial impact of capital expenses until their next general rate cases from both their ROE and ROR. Because PWW and PEU are entirely owned by a municipality, they do not have access to such equity capital in any manner, and therefore must borrow all funds needed to finance necessary annual capital investments.

The approved QCPAC mechanism allows PWW and PEU to establish a surcharge on its current permanent rates on an annual basis sufficient to support the additional debt service obligations arising from the new capital expenditures, as well as the associated property tax expenses for these new capital assets, incurred, funded, and requiring the initiation of repayment each year. PWW, PEU, and their lenders rely on this regular, consistent, and annual QCPAC process, as approved by the Commission, as part of its Ratemaking Structure to provide the loan financing necessary to support the annual capital investments required by the companies to meet their core, prudent and fundamental services as regulated water utilities.

While such a process is unique, PWW, PEU and its management team have been able to explain the QCPAC mechanism to its lenders and have been successful in accessing new borrowings on an annual and ongoing basis. Without the clear and consistent application of the QCPAC process to provide the rates necessary to repay new loans; however, lenders may have uncertainty as to whether PWW and PEU would ultimately obtain necessary revenues through the general ratemaking process to cover new debt service. Because PWW and PEU do not have access to equity, these lenders may determine that such loans are too risky and decide against extending the required credit to finance regular and recurring capital expenditures. The QCPAC process was intentionally designed to address these potential concerns by lenders and to enable PWW and PEU to access debt capital between general rate cases. I therefore request that the Commission continue and maintain this unique step process for the Pennichuck regulated companies, as it has approved other elements of the Companies' rate structures that are truly unique and cash flow based.

The QCPAC consists of: (1) the annual principal and interest payments with respect to the applicable capital project debt, multiplied by 1.1; and (2) incremental property taxes associated with the specific capital projects, as determined in the year of the granting of the QCPAC for such projects. The approved QCPAC process is calculated via annual filings, providing: (1) calculation of the QCPAC surcharge associated with capital investments from the previous year, for which all assets must be used and useful as of December 31 of that previous year; (2) budget information regarding proposed capital projects for the current year; and (3) a detailed forecast of anticipated capital project expenditures for the subsequent two years, for informational purposes only. Customers receive notices of the proposed surcharge within 30 days of the annual QCPAC filing.

The Department of Energy's Audit Division plays a crucial role in evaluation of the Company's QCPAC submissions, capital budgets and projects in determining the projects were prudent, used, and useful and placed in service during the prior year.

We have worked with the Commission and DOE staff, in recent settlement proceedings to streamline the process for the QCPAC mechanism. We believe the settlement process plays a key role, in conjunction with an Order Nisi approval process to ensure an efficient and timely approval of QCPAC surcharges to allow for recovery of capital expense debt service, interest and taxes.

I believe the current QCPAC criteria, as approved for PWW and PEU are appropriate and adequate and it is vitally important to point out that the QCPAC surcharges earned between rate case are adjusted to zero with each rate case filing for the respective companies to reconcile the rates. It is also important to note that both PWW and PEU, as addressed in settlements to recent rate cases for each entity in DW 19-086 and DW 17-128, are obligated to file full rate cases every three years. This modality of permanent rate filings was proposed by the Companies, agreed to by the parties to those dockets, and approved by the Commission. The significance of this was intended to do the following: (1) embed the QCPAC surcharges earned between full rate cases into new permanent rates, and (2) allow for the full examination of each Company's final performance, allowed rate structure, earnings versus allowed levels, and reassessment of the factor percentage in the Company's Material Operating Expense Factor (MOEF), as it pertains to cash flow coverage and Rate Stabilization Fund (RSF) adequacy for the OERR portion of its allowed revenues.

We would also like to point out that the Pennichuck regulated utilities, along other water utilities in New Hampshire, are subject to certain conditions that other regulated utilities (gas and electric) would not be impacted by, and for very important health-based reasons. Water utilities are providers of water needed to sustain life and/or avoid adverse health related symptoms or impacts, in compliance with EPA and NHDES Safe Drinking Water Standards. Water utilities must therefore comply with these regulatory requirements, including maximum contamination limits (MCLs) or treatment based standards, imposed by the EPA and NHDES, that are ever evolving and becoming more stringent. In addition, the ability to comply with these standards many times requires either capital investments or operational expense modifications for water utilities which are both significant and/or highly time sensitive. Based upon this, regulated water utilities in the State must have the financial ability and flexibility to properly maintain proper stewardship with regards to compliance with these health-based water standards. By totally eliminating the ability for water utilities to request and garner approval for step increases between full rate case proceedings, in order to comply with these important standards, would impact the ability of these utilities to provide residents in the State with safe drinking water.