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March 2, 2023

Via Electronic Mail

Ms. Carmen Diaz, Acting Secretary
New Jersey Board of Public Utilities
44 South Clinton Avenue, 9th Floor
P.O. Box 350
Trenton, New Jersey 08625-0350

**Re: In the Matter of the Petition of Pinelands Wastewater Company for
Authority to Issue and Sell up to \$4.9 Million of Principal Amount Debt
Securities
BPU Docket No.: WF22110696**

Dear Acting Secretary Diaz:

Please accept for filing these comments of the Division of Rate Counsel (“Rate Counsel”) regarding the above-referenced matter. Consistent with the March 19, 2020 *Order of the New Jersey Board of Public Utilities (“Board”) in I/M/O the New Jersey Board of Public Utilities’ Response to the COVID-19 Pandemic for a Temporary Waiver of Requirements for Certain Non-Essential Obligations*, BPU Docket No. EO20030254, copies of this comment letter are being filed electronically with the Secretary of the Board and provided electronically to each person on the service list. No paper copies will follow. Please acknowledge receipt of this comment letter. Thank you for your consideration and attention in this matter.

A. Background

Pinelands Wastewater Company (the “Company” or “Pinelands”) is a duly organized and existing public utility of the State of New Jersey subject to the jurisdiction of the Board. The Company is engaged in the business of collecting and treating wastewater to 2,450 customers in Southampton Township, Burlington County. The Company owns and operates certain collection

and treatment facilities for these purposes. The Company is a wholly owned subsidiary of Middlesex Water Company. The Company's 2021 revenues were approximately \$1.5 million.¹

On November 18, 2022, the Company filed a petition ("Petition") requesting the following approvals and authorizations from the Board:

- To enter and close a \$4.9 million long-term loan from CoBank, ACB ("CoBank") on the terms and conditions set forth in CoBank's Term Sheet dated October 27, 2022, attached to the Company's Petition as Exhibit G,
- To make, execute, and deliver to CoBank such instruments as required to evidence and secure the Loan, in accordance with its terms, and
- To obtain such other relief as the Board determines is just and proper.²

The Company's petition states that it expects to use the net proceeds from the CoBank loan to retire existing short-term debt, to fund capital expenditures to be incurred in its five-year Capital Program for the upgrade, replacement, and improvements to its wastewater system, and for other general corporate purposes.³ The Company requests the Board's authorization to accomplish the financing contemplated in the Petition at any time before December 31, 2026.⁴

B. Rate Counsel Analysis

In the past, the Company has received debt financing from its corporate parent, Middlesex Water Company, in the form of short-term, intercompany notes payable. For accounting purposes, notes payable are classified as short-term debt because they mature in less than one year. That is, the Company must refinance its short-term notes payable at least annually. As of September 30, 2022, Pinelands had \$2.2 million in notes payable outstanding to its corporate parent.⁵ This amount represented 47.07 percent of the Company's capitalization.⁶ Middlesex Water Company charges the Company 7 percent interest on its short-term loans.

Both the Company and Middlesex now wish to separate the Company's debt financing from the parent company. Both entities face an increasing demand and costs to replace their

¹ Pinelands Response to OE-8.

² Petition, page 4.

³ Petition, para. 9.

⁴ Petition, para. 2.

⁵ Petition, Exhibit A.

⁶ Pinelands response to RCR-PWW-11.

aging infrastructure.⁷ Middlesex, like the Company, is under pressure to expand its use of debt to finance its capital expansion program. Thus, the Company believes that now is the appropriate time to establish stand-alone, long-term debt. In turn, Middlesex believes that its own financial strength will benefit from the Company having its own stand-alone debt.⁸

The Company proposes to meet its debt financing requirements by entering into a loan agreement with CoBank. CoBank is a cooperatively owned financial institution that provides credit through leases and loans within rural markets. Given the amount of debt financing sought by the Company, approximately \$5 million, most financial intermediaries such as investment banks, insurance companies, mutual funds, etc. are not likely to be interested in providing financing to the Company. Such intermediaries typically prefer much larger issuances.⁹ Thus, CoBank seems better suited to meet the Company's long-term debt requirement. Moreover, Middlesex, through another corporate affiliate, Tidewater Utilities, Inc., has prior borrowing experience with CoBank.¹⁰ For water utilities within New Jersey, Gordon's Corner Water Company also receives debt financing from CoBank, which previously has been approved by the Board.¹¹

Rate Counsel does not oppose the Company's plan to make itself more financially independent from Middlesex. Obtaining its own debt financing also should lower financing costs for the Company and for customers as well. Middlesex has charged the Company 7 percent per annum interest on outstanding short-term notes payable. This amount substantially exceeds Middlesex's actual short-term debt costs and its recently approved embedded cost of long-term debt.¹² CoBank will establish the interest rate for a 20-year loan to the Company at the time of the transaction based on then-current market conditions. Unless debt markets go completely haywire by that time, CoBank's interest rate is likely to be considerably lower than the 7 percent rate that Middlesex currently charges the Company.

The Company's objective is to maintain a capital structure consisting of 53 percent common equity and 47 percent debt.¹³ The Company has maintained these approximate

⁷ Pinelands response to RCR-PWW-12.

⁸ *Ib.*

⁹ Pinelands response to RCR-PWW-3.

¹⁰ Pinelands response to RCR-PWW-4.

¹¹ *Ib.*

¹² Pinelands response to RCR-PW-18. Middlesex's cost of short-term debt as of September 30, 2022, was 3.7280%. In BPU Docket No. WR22090555, the Board approved a 2.68% average cost of debt for Middlesex.

¹³ Pinelands response to RCR-PWW-10.

capitalization ratios since September 2021.¹⁴ Rate Counsel offers no opinion on the reasonableness of the Company capital structure goals. Rather, the Company’s actual capital structure will be reviewed for reasonableness in the context of a base rate proceeding and not in this financing proceeding. The Company has considerable ability to achieve its capital structure goals, however, through long-term debt issuances, through retained earnings, and through equity infusions from Middlesex. The Company has an obligation to maintain an appropriate capital structure that balances its own financial risk and the customers’ desire for the least cost capital alternative.

CoBank’s Terms and Conditions require the Company to meet and maintain certain financial covenants to secure a loan.¹⁵ Specifically, CoBank requires the Company to have a Debt Service Coverage Ratio of greater than 1.40 times at each fiscal year end that the loan is outstanding and to maintain a Total Debt to Capitalization Ratio of not greater than 65 percent at each fiscal year end.¹⁶ Following are the Company’s Debt Service Coverage Ratios and Total Debt to Capitalization ratios for the years 2017 through 2021.¹⁷

	Coverage	Capitalization
2017	6.81	34.45%
2018	5.12	31.43%
2019	5.48	31.26%
2020	11.03	27.77%
2021	4.36	48.12%

These figures demonstrate that historically the Company’s debt service coverage and capital structures have been sufficient to satisfy CoBank’s financial covenants. Thus, for the near term at least there appears to be minimal risk that the Company will not be able to meet its service obligations on the newly acquired long-term debt. This is despite the Company’s testimony in its recent base rate proceeding concerning Pinelands “...inability to demonstrate that it has the net income and cash flow to support debt repayment.”¹⁸

¹⁴ Pinelands response to RCR-PWW-11.

¹⁵ Petition Exhibit G, pages 4 and 7.

¹⁶ *Ib.*

¹⁷ Pinelands response to RCR-PWW-9.

¹⁸ Pinelands Water Exhibit P-4, Direct Testimony of Michele L. Tilley, page 11, BPU Docket No. WR22090555.

C. Rate Counsel Recommendation

Rate Counsel has carefully reviewed the Petition and is not opposed to its approval. The Company is engaged in the distribution of water 2,500 customers in its New Jersey service territory. The proposed financing is necessary and appropriate as part of the Company's overall strategy to provide safe, adequate, and reliable service to its New Jersey customers. Barring unforeseen and unanticipated circumstances, the proposed debt issue should not jeopardize the Company's financial integrity. Based on the Company's recent financial performance, it appears that the Company has sufficient income to meet additional debt service interest requirements without jeopardizing its ability to provide safe, adequate, and reliable service to its New Jersey customers.

Even though Rate Counsel is generally supportive of the authorizations sought in the Petition, approval of the Petition should not include an authorization to include in rate base any specific assets that will be acquired as a result of this financing. Nor should the Board's authorization in this Petition be construed as acceptance for future ratemaking purposes of the resulting capital structure and capital costs. The determination of any assets to be included in rate base and the ratemaking impact of serving customers, including the impact of the transaction(s) on the Company's capital costs will be addressed in a future base rate proceeding.

Rate Counsel recommends that the Petition be approved with the following conditions:

1. The Board's approval is expressly limited to the loan described in the Petition. In the event the loan transaction with CoBank is not consummated, for any reason, the Company may not obtain financing from any other lender until the approval by the Board has been obtained.
2. No franchise rights will be capitalized directly or indirectly by the issuance of the bonds.
3. Approval by the Board shall not be construed as directly or indirectly fixing, for any purpose, any value of the tangible or intangible assets now owned or hereafter to be used by Pinelands; nor as certifying that the securities authorized to be issued and sold will be represented by tangible or intangible assets of commensurate value or investment cost.
4. The Board's approval shall not indicate authorization to include in rate base the specific assets that will be constructed or acquired as a result of the Petition. The determination

of any assets to be included in rate base and the rate making impact thereof shall be addressed in a future base rate proceeding.

5. Approval by the Board shall not affect or in any way limit the exercise of the authority of the Board or of the State of New Jersey in any future petition or in any proceeding with respect to rates, franchises, services, financing, accounting, capitalization, depreciation, or in any other rate matters affecting Pinelands.
6. Pinelands shall submit a schedule indicating complete details of the issuance costs no later than sixty (60) days following the closing date for this transaction.
7. Pinelands shall furnish the Board with copies of the executed indentures.
8. The authority granted by the Board shall become null and void and of no effect if not exercised by December 31, 2026.

These provisions will satisfy Rate Counsel's concern that the Board's approval is limited to the transactions as described herein, does not imply authorization to include any specific assets or amounts in rate base, does not imply authorization for any other ratemaking treatment, and does not establish any precedent with regard to approval of future financing petitions.

Respectfully Submitted,

Brian O. Lipman, Esquire
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By: *Susan E. McClure*
Susan E. McClure, Esquire

C: Service List

**I/M/O the Application of Pinelands
Wastewater Company For Authority
to Issue and Sell up to \$4.9 Million of
Principal Amount Debt Securities**

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