

REBUTTAL TESTIMONY
OF
MAUREEN E. GURGHIGIAN
MANAGING DIRECTOR
FIRST SOUTHWEST COMPANY
ON BEHALF OF THE CITY OF NEWPORT, UTILITIES DEPARTMENT, WATER
DIVISION

In re: City of Newport Utilities Department, Water Division

Docket No. 4243

September 21, 2011

1 **Q. Please state your name and business address.**

2 A. My name is Maureen E. Gurghigian and I am a Managing Director at First
3 Southwest Company's Lincoln, Rhode Island office.

4
5 **Q. Please describe your education and experience.**

6 A. I hold a Masters Degree in business administration from the University of Rhode
7 Island. I am a registered Municipal Principal with the Municipal Securities
8 Rulemaking Board, holding the following licenses: Series 52, Series 53 and Series
9 63. Prior to joining First Southwest in 2001, I worked in public finance for Fleet
10 Bank and/or Fleet Securities for 16 years. From 1993 through 2000, I served as
11 Manager of New England Investment Banking at Fleet Securities, Inc. Before
12 joining Fleet, I spent 8 years in Rhode Island State Government, including four
13 years as Director of the Governor's Policy Office under then Governor J. Joseph
14 Garrahy.

15

16 **Q. Can you describe First Southwest Company and the types of services it provides?**

17 A. Since 1946, First Southwest Company has served as financial advisor to many
18 issuers such as schools, cities, airports, hospitals, sports complexes, water and
19 wastewater authorities and districts and toll roads. Currently the firm serves more
20 than 2,000 municipalities and agencies, including more than 400 in New England.

21

22 **Q. Can you please describe your duties at First Southwest Company.**

23 A. I provide financial advisory services to issuers of municipal debt, primarily in the
24 State of Rhode Island. Annually, I am involved in more than 20 publicly offered
25 bond issues. In addition, I have supervisory responsibility for First Southwest's
26 involvement with borrowings by the State of Rhode Island, numerous public

1 agencies and 30 Rhode Island municipalities. Our office assists clients with the
2 origination of more than \$800 million in public financing issues each year.

3
4 **Q. Have you previously testified before the Public Utilities Commission and Division
5 of Public utilities on rate related matters?**

6 A. Yes, I have testified before the Public Utilities Commission and the Division of
7 Public Utilities and Carriers on behalf of the Narragansett Bay Commission,
8 Woonsocket Water Division, Pawtucket Water Supply Board and the City of
9 Newport, Utilities Division, Water Department (“Newport Water”).

10
11 **Q. Please describe your role in this proceeding.**

12 A. I am assisting Newport Water and its financing team with the issuance of debt to
13 fund improvements to Newport Water’s Station One Treatment Plant and the
14 construction of a new water treatment plant at Lawton Valley (collectively
15 “Treatment Plant Projects” or “Projects”). Newport Water asked me to testify as a
16 rebuttal witness in this matter regarding its request to increase debt service
17 funding for the Treatment Plant Projects.

18
19 **Q. How much does Newport Water need to borrow for the Treatment Plant
20 Projects?**

21 A. Newport needs to borrow more than \$86 million between FY12 and FY14 to fund
22 the Treatment Plant Projects. It is my understanding that Newport Water seeks a
23 multi-year increase in this docket to phase in the debt service increases required
24 to finance the Treatment Plant Projects.

1 **Q. How does Newport plan to seek this financing?**

2 A. Ideally, Newport Water would like to completely fund the Projects through the
3 Rhode Island Clean Water Finance Agency (“RICWFA”). As the Commission knows,
4 the State of Rhode Island created a Drinking Water State Revolving Fund
5 (“DWSRF”) administered by the RICWFA to provide financial assistance to water
6 suppliers in accordance with the Safe Drinking Water Act Amendments of 1996.
7 This fund uses federal capitalization grants and state matching funds to provide
8 subsidized (25% below market-rate) loans to water suppliers for qualifying projects
9 listed on the Project Priority List maintained by the Department of Health. The
10 RICWFA sells bonds in the public market and loans the proceeds to its drinking
11 water borrowers pursuant to loan agreements. The DWSRF currently provides a
12 significant portion of funding for Newport Water’s ongoing capital program.

13
14 Newport Water identified the Treatment Plant Projects in its capital program, and
15 they are listed on the Rhode Island Department of Health’s Project Priority List.
16 Therefore, the projects qualify for subsidized DWSRF loans through RICWFA.

17
18 **Q. Will Newport be able to fund the entire cost of the Treatment Plant projects
19 through the DWSRF?**

20 A. It is anticipated that the DWSRF will fund at least part of the Treatment Plant
21 Projects. Unfortunately, the RICWFA cannot guarantee complete funding for the
22 Treatment Plant Projects. Due to the size of the Projects and the amount of money
23 needed, the RICWFA may not have enough capacity to provide 100% of the
24 required financing. The DWSRF capacity is driven by the level of capitalization
25 grants provided by the federal government. Proposed cuts in federal funding will
26 result in fewer subsidized loans for borrowers such as Newport Water. The

1 RICWFA reviews its capacity on an annual basis and takes into account the
2 projected funding level as well as the needs of prospective borrowers.

3

4 **Q. What are Newport's options if it cannot completely finance the Treatment Plant**
5 **Projects through the RICWFA and the DWSRF?**

6 A. Newport would need to seek unsubsidized financing for any portion of the
7 Projects that the RICWFA cannot fund through the DWSRF. Newport's options
8 would include:

9 1. Borrow through the RICWFA on an unsubsidized or market rate basis. A
10 market rate loan from RICWFA would work very much like the conduit loans
11 Newport and other RICWFA borrowers have undertaken for non-SRF eligible
12 projects. RICWFA would sell a bond issue only on behalf of Newport and
13 Newport would pay the market rate.

14

15 2. Under current law Newport can only sell revenue bonds to RICWFA.
16 Newport could introduce legislation in the Rhode Island General Assembly
17 allowing it to issue revenue bonds directly to the public markets.

18

19 Under either scenario, market rate bonds would not provide the same discounted
20 interest rate as the DWSRF. However, they would allow Newport to obtain the
21 necessary funding if the RICWFA has insufficient lending capacity for the entire
22 Treatment Plant Projects. Other borrowers that have a combination of market rate
23 and subsidized loans include the Pawtucket Water Supply Board and the
24 Narragansett Bay Commission.

25

1 **Q. Did you review the direct testimonies of Thomas Catlin submitted by the Division**
2 **of Public Utilities and Carriers and Christopher Woodcock submitted by the**
3 **Portsmouth Water and Fire District regarding Newport's request for debt service**
4 **funding?**

5 A. Yes, I did. I also reviewed Harold Smith's rebuttal testimony on this issue.
6

7 **Q. Do you believe that Mr. Smith's rebuttal position regarding debt service is**
8 **reasonable?**

9 A. Yes. I do. It is my understanding that Mr. Smith delayed the multi-year increase
10 Newport requested. According to Mr. Smith, Newport will not need to make debt
11 service payments in the Rate Year to fund the Projects because of the schedule for
12 selecting a vendor and starting construction. I also believe that Newport's
13 continued use of 6% interest rate and a modified 12% cost of issuance is
14 reasonable given the time horizon for the borrowings.
15

16 **Q. Can you explain why a 6% interest rate and a 12% cost of issuance is reasonable?**

17 A. Yes. As set forth in my testimony above, we do not know how much of the
18 Treatment Plant Projects can be funded through the DWSRF. Thus, it is possible
19 that Newport will use unsubsidized borrowing for a portion of the Projects.
20 Further, the borrowings will be done over three fiscal years. The current Bond
21 Buyer Revenue Bond Index was 5.15% on September 1, 2011. The median for the
22 past 12 months has been 5.35% and today's tax exempt rates are at historical
23 lows. Since the borrowings will take place over a multi-year period, I believe that
24 modeling at 6.0% is prudent. Should the interest rate for the initial loan be less
25 than 6.0%, future increases required for subsequent loans would be lower.
26

1 As for the cost of issuance, I am comfortable with Newport's revision to 12%. I
2 believe that any further reduction would be unreasonable at this point. The major
3 portion of the 12% is the debt service reserve fund which is sized at 10% of par or
4 maximum annual debt service, whichever is lower. Since a market rate loan would
5 result in higher debt service, it is prudent to model the debt service reserve fund
6 at 10%. Based on recent experience, we would expect the other costs of issuance
7 would range from 1.5% to 2.0% depending upon the size of the loan. In addition,
8 the Treatment Plant Projects include the expense for a Feasibility Study that is not
9 required for other DWSRF loans.
10

11 **Q. Are the 6% interest rate and 12% cost of issuance unreasonably conservative?**

12 A. No. It is important for Newport to have enough funds in place as it embarks on
13 these major capital projects. It is my understanding that the Commission must
14 review Newport's multi-year plan each time a successive increase is scheduled to
15 take effect. If Newport is able to fund a larger portion of the Projects through the
16 DWSRF, or if unsubsidized rates are lower than projected, then successive
17 increases can be reduced or otherwise modified. This is preferable to Newport not
18 having enough to service its debt if rates increase or the RICWFA's capacity is
19 curtailed. Bond rating agencies and investors will look at Newport's projected rates
20 and debt service coverage very carefully. Smoothing out rate increases for a multi-
21 year capital program is viewed positively by rating analysts. It is especially
22 important for Newport to maintain its bond rating as it initiates such a major
23 capital program since any negative rating action would result in much higher
24 interest costs, particularly for market rate loans.
25
26

- 1 **Q. Does this complete your testimony?**
- 2 A. Yes it does.

CERTIFICATION

I hereby certify that on September 21, 2011, I sent by electronic mail a copy of the within to Service List herein below, and mailed one original and nine copies to Luly Massaro, Clerk, Rhode Island Public Utilities Commission.

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