

SUMMARY OF THE CITY OF NASHUA'S ACQUISITION AND OWNERSHIP OF PENNICHUCK CORPORATION

This summary is prepared by Pennichuck Corporation to provide history and background information about the City of Nashua's ownership and the operation of Pennichuck and its three water utilities, including Pennichuck Water Works, Inc. For further information, please contact the Company's Chief Executive Officer who can be reached during business hours at Pennichuck's general phone number, (800) 553-5191. Also visit the Company's website (www.pennichuck.com) for information relative to the Company and its subsidiaries.

History

The City of Nashua, New Hampshire (the "City") acquired the shares of Pennichuck Corporation ("Pennichuck") on January 25, 2012 and became the sole shareholder of the Company. This transaction resolved a decade-long dispute with Pennichuck over the rising cost of water service and control over important water services and watershed land.

While this dispute began in the early 2000s with the City's effort to purchase Pennichuck's assets by eminent domain, it was ultimately resolved on a consensual basis following successful negotiations between a team of City representatives led by then Mayor Donnalee Lozeau and representatives of Pennichuck Corporation.

The transaction enjoyed a broad range of public support from the City's residents, its elected leaders, State regulators and, indeed, the State Legislature. This broad public support included the enactment of special legislation by the State Legislature in 2010, unanimous approval of the transaction by the Mayor and Board of Aldermen in January 2011, and approval by the New Hampshire Public Utilities Commission in November 2011.

The City's purchase of the shares of a previously for-profit, investor-owned corporation – which had been publicly traded on the NASDAQ stock exchange – represents a creative and unique transaction intended to provide lower water service costs over time than that provided by the publicly-traded corporation for customers located in Nashua and other communities served by the three Pennichuck regulated water utilities, and to provide careful and stable public control over important watershed land and environmental interests.

Transaction Completed

The transaction was accomplished in accordance with a corporate merger agreement executed on November 11, 2010, pursuant to which the City acquired all of the outstanding shares of Pennichuck for \$29.00 per share or a total purchase price of \$138 million. The City financed the costs of the transaction by issuing 30-year General Obligation Bonds in the total amount of \$150.6 million.

The proceeds of this bond issuance were provided to the New Pennichuck Corporation in the form of a loan and an equity investment. These funds were used as shown in the following table:

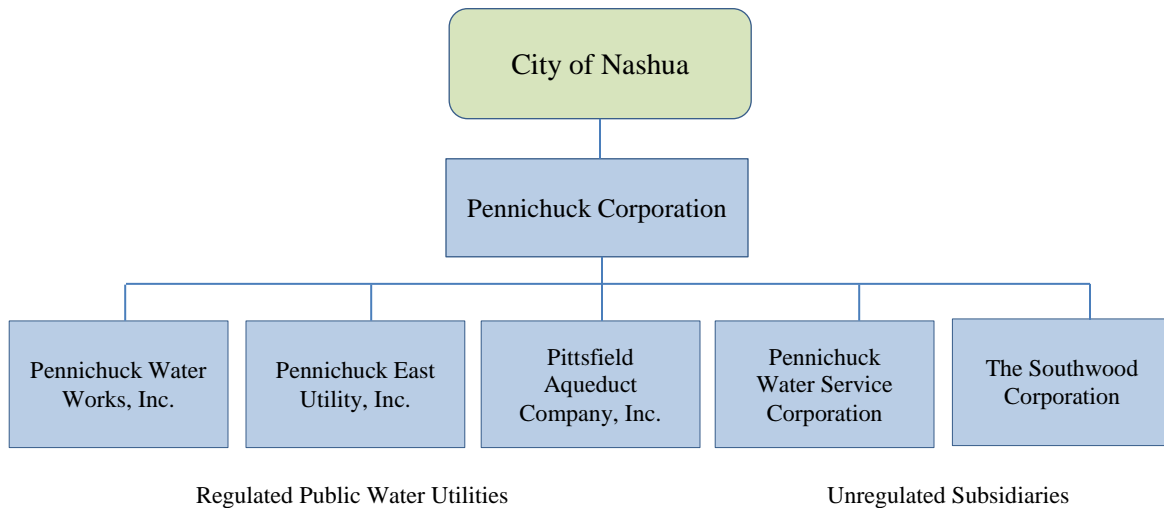
Summary of Sources and Uses of Financing Proceeds in Pennichuck Transaction ¹

Sources of Funds	(\$ millions)	Uses of Funds	(\$ millions)
Loan to New Pennichuck	120.6	Consideration Paid for Shares	138.4
Equity Investment in New Pennichuck	30.0	Bond Issuance Costs and Fees	1.0
		Transaction Costs and Fees	3.9
		Severance Costs	2.3
		Funding the Rate Stabilization Fund	5.0
<u>Total Sources of Funds</u>	<u>150.6</u>	<u>Total Uses of Funds</u>	<u>150.6</u>

Corporate Ownership Structure

Today, the City continues to own all of the outstanding shares of Pennichuck, and serves as the Sole Shareholder of the Company. Pennichuck Corporation itself is a holding corporation, whose principal assets are the shares of five corporate subsidiaries. Three of these subsidiaries are regulated public water utilities: Pennichuck Water Works, Inc.; Pennichuck East Utility, Inc.; and Pittsfield Aqueduct Company, Inc. The two remaining subsidiaries are unregulated: Pennichuck Water Service Corporation (which provides operations and management services for several other communities and independently-owned small water systems) and The Southwood Corporation (which owns various parcels of land in Merrimack, New Hampshire).

The following diagram illustrates this corporate ownership structure:



¹ The share consideration reflects \$29.00 per share owned by public shareholders, plus adjustments for share options outstanding at the time of the transaction. Bond issuance costs include bond counsel and financial advisor fees and other costs of issuing the City bonds. Transaction costs include legal and accounting fees, investment banking fees, and the City's due diligence costs. Severance costs include payments to senior management persons who were terminated as a result of the transaction, pursuant to their Change in Control agreements. The Rate Stabilization Fund is held by Pennichuck Water Works, Inc. as a reserve to ensure stable revenues in adverse periods.

Corporate Governance

Pennichuck and its subsidiaries continue to operate as corporations, in accordance with longstanding corporate governance principles intended to promote good business decisions, made with transparency and accountability. Pennichuck and its utilities are not municipal departments or water districts.

As a corporation, Pennichuck's operations are carried out in accordance with actions approved by the City, in its capacity as the Sole Shareholder of the Company, with actions approved by Pennichuck's Board of Directors with members elected by the Sole Shareholder, and actions implemented by Pennichuck's management and employees. Like any other corporation, Pennichuck's activities are governed in accordance with rules established by general principles of corporate law, its Articles of Incorporation, and its Bylaws. These documents, which are available on Pennichuck's website and upon request, were developed by the Mayor and the Board of Aldermen at the time of the transaction, and the Bylaws have been amended since then.

Pursuant to Pennichuck's Articles of Incorporation and Bylaws, the City's Mayor and Board of Aldermen, acting in the City's capacity as the Sole Shareholder, has certain powers. The Sole Shareholder elects all members of Pennichuck's Board of Directors, and determines compensation for Board members. In addition, Pennichuck may not take any of the following actions without the prior approval of the Sole Shareholder:

- to change the name of the Company or of any of its subsidiaries;
- to amend the Bylaws of Pennichuck or any of its subsidiaries;
- to approve borrowing by Pennichuck or its subsidiaries, including guarantees;
- to approve mergers;
- to approve the sale, lease, transfer or disposal of all or any substantial part of the assets of Pennichuck or any of its subsidiaries other than in the ordinary course of business; and
- to approve any investments in stock.

In general, Pennichuck's management team provides the day-to-day operations. The Board of Directors, which must act in accordance with the Articles of Incorporation and the Bylaws, provides oversight of the management team. Pennichuck's Bylaws provide specific rules on the number and qualifications for the Board of Directors. These requirements include:

- the Board will consist of at least seven, but no greater than thirteen members;
- the Board will have at least five members who are residents of the City, one non-resident of the City who is also a customer, and one member who is nominated by the Merrimack Valley Regional Water District;
- a Board member serves for a three-year term, and terms are staggered; and
- the Board cannot include any member who is:
 - Mayor of the City (other than in the first two years following the January 25, 2012 transaction date);
 - a member of the City Board of Aldermen;

- an elected member of a governing body of any municipality with residents served by Pennichuck utilities;
- the City's Public Works Director or member of the City's Public Works Committee;
- any person who served in one of the above categories during the 2-year period prior to election to the Board; or
- any family member of any person described above.

In order to be elected to serve on the Pennichuck Board of Directors, a qualifying person must first be nominated by the Nominating and Governance Committee of the Pennichuck Board (or, in the case of the single position, by the Merrimack Valley Regional Water District). Nominees are then subject to approval by the full Pennichuck Board of Directors, and finally to election by the Sole Shareholder at the Annual Meeting of the Sole Shareholder.

Regulated Utilities

Today, the City continues to own all of the outstanding stock of Pennichuck's three regulated public water utilities through its ownership of Pennichuck.

- Pennichuck Water Works, Inc. provides water service to approximately 27,600 customers in 11 New Hampshire communities, which include Amherst, Bedford, Derry, Epping, Hollis, Merrimack, Milford, Nashua, Newmarket, Plaistow and Salem.
- Pennichuck East Utility, Inc. provides water service to approximately 7,100 customers in 19 New Hampshire communities, which include Atkinson, Barnstead, Bow, Chester, Conway, Derry, Exeter, Hooksett, Lee, Litchfield, Londonderry, Middleton, Pelham, Plaistow, Raymond, Sandown, Tilton, Weare and Windham.
- Pittsfield Aqueduct Company, Inc. provides water service to approximately 600 customers in Pittsfield, New Hampshire.

Regulation by New Hampshire Public Utilities Commission

As corporate utilities, each of these three utilities is subject to regulation by the New Hampshire Public Utilities Commission (the "NHPUC"). The NHPUC must approve all water rates charged by the utilities, all borrowings by the utilities, and various other transactions.

As part of the NHPUC's approval of the City's transaction, the NHPUC approved a rate structure that would treat customers fairly and provide the regulated utilities with necessary revenues to provide high quality water service and to allow the City to repay the bonds it issued to complete the transaction. This rate structure allows the utilities to charge rates comprised of two parts: (1) a "fixed component" that ensures revenues to repay the City's bonds (known as the "City Bond Fixed Revenue Requirement" or "CBFRR", approximately \$8.8 million per year); and (2) an "operating component" that ensures revenues to cover customary and essential operating costs, including depreciation and amortization. Pennichuck's funding of the City's repayment of the bonds takes the form of principal and interest payments on the note payable to the City and quarterly dividends paid to the City.

Assumptions and Projections Regarding the City's Acquisition of Pennichuck

When it purchased the shares of Pennichuck, the City developed, with the assistance of its advisors, detailed financial models based on various assumptions regarding inflation, water consumption, and other factors. These models projected results under the City's ownership. These models were provided to the Mayor and Board of Aldermen as they deliberated on whether to approve the transaction.

Based on the purchase price and the assumptions, these models projected that increases in future water rates for customers would be lower under the City's ownership for two main reasons:

- Under the special rate structure, the utility would only seek to charge rates sufficient to allow the City to repay its bonds, while an investor-owned utility would seek to charge rates that included a profit on equity investment (equity profits are higher than interest payments on debt such as the City bonds).
- Under the City's ownership, Pennichuck and its utilities would be able to decrease annual operating costs by eliminating the costs of being a publicly-traded company and costs of certain senior management positions that were either eliminated or replaced as a result of the transaction.

The major assumptions in the financial models provided to the Mayor and Board of Aldermen prior to the transaction included:

- rate increases in 2013 could be 2.01%;
- rate increases for each year thereafter could be as high as 2.9%;
- general inflation for operating costs would increase at 3.0% annually;
- cash flow would be sufficient to repay the City's acquisition bonds (\$150.6 million);
- capital expenditures would be \$8 to \$10 million per year in 2012, increasing with inflation to approximately \$17 million in 2042; and
- capital expenditures would be financed entirely by new borrowings.

Rate Stabilization Fund

An important part of the City's transaction of Pennichuck was the establishment of a \$5 million "Rate Stabilization Fund" ("RSF"). This RSF was established in order to provide a type of reserve fund that could be drawn upon to meet obligations for the City's bonds during periods of unexpected declines in regulated utility revenues. If actual utility revenues are lower than expected, then Pennichuck may "draw down" funds from the RSF to meet its fixed obligations to the City. Conversely, if actual utility revenues are higher than expected, Pennichuck will deposit a share of the higher revenues into the RSF. In subsequent rate cases, customer rates will be adjusted to return any RSF excess over \$5 million to customers or to replenish any RSF deficit below \$5 million through increased rates.

Eminent Domain Cost

The City expended approximately \$5 million on the eminent domain case which preceded the negotiation of the transaction. The Order issued by the New Hampshire Public Utilities Commission allows the repayment of the City's eminent domain cost if there are sufficient profits after the payment of the CBFRR. Such a payment cannot exceed \$500,000 per year.