***Consumers Council of Canada and the Vulnerable Energy Consumers Coalition (CCC) and (VECC) INTERROGATORY #27 List 1***

***Interrogatory***

Ref: B1/T3/S1 p. A-3

Issue 4.0
Issue: Cost of Capital/Capital Structure

Topic: Book Values

Request:

a) Please provide references to the "some" who would argue that the market value of utility shares should equal their book value and sketch out the major theoretical reasons why this should be so.

b) Would Ms. McShane agree that as long as utility assets can only be used to provide service their replacement cost is immaterial. Further would Ms. McShane agree that as long as assets are included in the rate base if prudently acquired the investor is not at risk for the capital invested in the utility even if the replacement cost turns out to be much lower?

c) Is Ms McShane aware that purchaser of electricity in Ontario is paying a debt retirement charge that in part reflects stranded debt costs attached to nuclear energy and that consumers would not pay this charge in a competitive market.

***Response***

a) The reference to "some" includes economists or cost of capital witnesses (e.g., Dr. Booth, who has given evidence on numerous occasions before the OEB) who take the position that (1) the original cost of the assets reflects the amount of capital that investors have committed; (2) investors are only entitled to a return on the dollars of capital that they committed; (3) the equity return to which they are entitled is equal to the current cost of equity; (4) the application of the current cost of equity to the original cost book value of the equity will maintain the market value of the equity at the amount of the capital that was originally invested; and (5) if the market value exceeds the book value, the utility is earning more than its cost of equity.

b) No, Ms. McShane does not think their replacement cost is immaterial. No, Ms. McShane does not agree with the conclusion that utility investors do not bear any

risk for the capital invested in the utility if the replacement cost turns out to be much lower.

c) Yes, she is aware of the debt retirement charge. She agrees that, under competition, consumers would not pay costs in excess of the price established by competitive markets.