Consumers Council of Canada and the Vulnerable Energy Consumers Coalition (CCC) and (VECC) INTERROGATORY #13 List 1

Interrogatory

Ref: B1/T3/S1 p. 34

Issue 4.0
Issue: Cost of Capital/Capital Structure

Topic: Allowed ROE

Request:

Ms. McShane recognises "the debt rating as an indicator or relative risk."

a) Does it then follow that utilities with lower bond ratings than Tx are riskier? Please explain why yes or no in detail;

b) If the answer is yes then please explain why Tx should be allowed a higher ROE than firms on an automatic adjustment mechanism that are currently earning lower allowed ROEs.

c) Please indicate the 2007 allowed ROE for "benchmark" utilities in BC, Alberta, Manitoba, Ontario, and Quebec.

d) In Ms. McShane's view are Ontario Discos more or less risky on average than TX, specifically is Ontario Hydro more or less risky?

e) If Ontario Electric distributors (Discos) have their allowed ROE set by the OEB adjustment formula is it "fair and reasonable" that Tx earn a higher ROE? Please explain in detail.

Response

a) Ms. McShane agrees generally with that proposition, with the caveat that the ratings of Hydro One are not purely stand-alone ratings; they reflect the strength of the shareholder.

b) The returns that the utilities on automatic adjustment mechanisms are allowed to earn are lower than what is fair and reasonable. Moreover, as discussed in Ms. McShane's testimony, the returns allowed for other Canadian utilities operating with automatic adjustment mechanisms do not constitute the only comparable

companies for purposes of assessing the reasonableness of the proposed return on equity and capital structure.

c) The 2007 allowed ROEs are below. To Ms. McShane's knowledge, the automatic adjustment formula is no longer in operation in Manitoba.

	Decision Date	Order/File Number	ROE(%)
Terasen Gas (BC)	3/06; 12/06	G-14-06; L-75-06	8.37
ATCO Electric (Alberta)			
Transmission	7/04; 11/06	2004-052; U2006-292	8.51
Distribution	7/04; 11/06	2004-052; U2006-292	8.51
Enbridge Gas Distribution (Ontario) [1/]	1/04; 2/06	RP-2002-0158; EB-2005-0001 EB-2005-0437	8.74
Gaz Metropolitain (Quebec)	9/06	D-2006-140	8.73

[1/] Return is for 2006; return based on December 2006 Consensus Forecast would be 8.34%.
Source: Board Decisions.

d) In the aggregate, she would consider the distributors to be of somewhat higher risk than Tx.

e) As indicated in response to J.9.55, the framework set out by the Board in its December 20, 2006 report was the result of a generic technical conference process for the LDCs, rather than the result of a full testing of evidence. The framework for the LDCs set out in the Board report is essentially a default position. Each LDC has the ability to bring its own evidence on cost of capital when it has its rates rebased.

HONI Tx is filing cost of capital evidence specific to its own circumstances, which is subject to a full evidentiary process. In that process, HONI Tx expects that the Board will take account of the various indicators that support the conclusion that the default position produces results that do not meet the standard of comparability of returns.