Q. Reference Evidence of Laurence Booth dated September 25, 2018

Page 47: Dr. Booth makes a second adjustment to his CAPM estimate which adds a .80% spread. Is Dr. Booth aware of any Canadian regulator that has applied or considered applying such an adjustment in their ROE conclusions? If yes, provide details of such decision.

A. Yes. The BCUC in its May 10, 2013 Decision (BCUC-GCOC-Stage 1, pages 90-91) stated

$$ROE_1 = \text{Base ROE } (8.75\%) + 0.50 \times (LCBF_t - BaseLCBF) + 0.50 \times (UtilBondSpread_t - BaseUtilBondSpread)$$

Where:
LCBF$_t$ is the Long Canada Bond Forecast for the test year, with a floor of 3.8 percent. The Base LCBF is 3.8%.
UtilBondSpread$_t$ is the average spread of 30 year A-rated Canadian Utility bond yields over 30 year Government of Canada bond yields and BaseUtilBondSpread will be determined.

6.3.3 Impact of a 3.8 percent Floor

FBCU has argued that the AAM proposed by Dr. Booth is biased downwards. The Commission Panel agrees that the potential for a downward bias does exist.

Dr. Booth has recommended that any change in the ROE be subject to a minimum forecast bond yield of 3.8 percent as this is the lowest rate which is consistent with a normal cyclical low. The Commission Panel accepts this as reasonable since it is the risk free rate for the CAPM ROE as determined in Section 5.2.

This 3.80% is the same trigger I have recommended to others.

Dr. Booth made similar recommendations before this Board in its 2013 Decision (PU 13(2013) where the decision on page 23 states, The range of recommended risk-free rates is 2.73% - 3.80%. Dr. Vander Weide adopts a rate of 2.73% but does not reflect the 2014 forecast and does not use the most recent forecast for 2013. Ms. McShane uses 3.50% but does not consider the most recent forecast and does not use the Consensus Economics forecast for 2013. Mr. MacDonald and Dr. Booth agree that the forecast long-term Canada bond yield for 2013 and 2014 is approximately 3.00%. Dr. Booth makes an adjustment to the forecast yield to reflect the impact of the actions of global policy makers. Dr. Booth applies an 80 basis point adjustment and determines a risk-free rate of 3.80%. Mr. MacDonald does not adjust the risk-free rate specifically but ultimately increases his capital asset pricing model result to address concerns regarding the impact of the abnormally low risk-free rate.

The Board accepts that the forecast long-term Canada bond yield is approximately 3.0%. The Board also accepts that this forecast is abnormally low and reflects the actions of global policy makers. Because the forecast may not accurately reflect the risk verses return trade-off by ordinary investors, the Board finds that an unadjusted forecast long-term Canada bond yield may not be a good proxy for the risk-free rate at this time. The Board accepts Dr. Booth's 80 basis point adjustment to the long-term Canada bond yield to reflect these unusual conditions.

Here the decision is explicit that the forecast LTC yield at the time was 3.0% but the decision is based on a 3.8% LTC yield, which was my 0.80% "Operation Twist" adjustment plus the 3.0% LTC yield forecast.