

1 **Q. (Application Volume 1, pages 3-42 and 3-43) It is stated “Mr. Coyne recommends a**
2 **fair rate of return on equity for Newfoundland Power of 9.8% based upon a capital**
3 **structure with a 45% common equity component.” The September 23, 2020**
4 **presentation by Fortis Inc. titled 2021-2025 Five-Year Outlook Conference Call**
5 **provides the following: i) Fortis BC Electric - 9.15 ROE on 40% equity, ii) Fortis**
6 **Alberta (electric) - 8.5% ROE on 37% equity, iii) Maritime Electric - 9.35% ROE**
7 **on 40% equity, and iv) Fortis Ontario - 8.52% - 9.30% ROE on 40% equity.**

- 8 a) **Please explain why it is appropriate for NP to have an equity component of**
9 **45% when these Canadian Fortis companies have equity components that**
10 **are 40% or less.**
11 b) **What return does Mr. Coyne recommend for a capital structure with a 40%**
12 **common equity component?**
13 c) **What return does Mr. Coyne recommend for a capital structure with a 37%**
14 **equity component?**

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16 A. a) Fortis Inc.’s regulated subsidiaries, including FortisBC, FortisAlberta, Maritime
17 Electric and FortisOntario, operate on a standalone basis and are each provided
18 the opportunity to earn a fair return, as determined by their local regulators. The
19 fair return is based on each utility’s unique set of risks and business
20 characteristics, regardless of affiliations with Fortis.

21
22 The Board has affirmed the fair return principle, indicating that to be considered
23 fair the return must be: (i) commensurate with the return on investments of similar
24 risk; (ii) sufficient to assure financial integrity; and (iii) sufficient to attract
25 necessary capital.¹ In assessing these requirements, the Board considers the
26 financial and business risk of a utility.

27
28 The Cost of Capital Report prepared by Concentric Energy Advisors (the
29 “Concentric Report”) provides an analysis of Newfoundland Power’s financial
30 risk and business risk. The Concentric Report concludes that “*the current*
31 *deemed common equity ratio for Newfoundland Power of 45 percent remains the*
32 *minimum appropriate level given these relative financial and business risks.*”²

33
34 In addition to the fair return standard, the standalone principle is a fundamental
35 concept of utility regulation. The Concentric Report describes the standalone
36 principle as follows:

37
38 *“The Stand-Alone Principle provides that the utility must be*
39 *regulated as if it were a stand-alone entity, raising capital on the*
40 *merits of its own business and financial characteristics. In this*
41 *way, capital may be efficiently allocated, with each business*
42 *segment earning a return based on its own unique set of risks and*

¹ Order No. P.U. 18 (2016), pages 10-11.

² See the 2022/2023 General Rate Application, Volume 3, Expert Evidence, Cost of Capital, page 79.

1 *business characteristics regardless of affiliations within the*
2 *holding company structure.*”³ [emphasis added]
3

4 The Board has upheld this principle and concluded that, in the interest of both the
5 utility and its customers, Newfoundland Power should be treated as a standalone
6 utility.⁴ As such, the affiliation between Newfoundland Power and FortisBC,
7 FortisAlberta, Maritime Electric and FortisOntario is not a relevant consideration
8 in determining the appropriate capital structure and return for each utility.
9

10 Additionally, Newfoundland Power’s financial and operational independence is
11 viewed as a credit positive by rating agencies,⁵ as is its capital structure, which
12 positively impacts its credit worthiness.⁶
13

- 14 b) Mr. Coyne was engaged by Newfoundland Power to provide an estimate of the
15 cost of capital for Newfoundland Power for the purpose of establishing the ROE
16 and capital structure for ratemaking purposes. As described in part (a),
17 Mr. Coyne recommended the common equity ratio of 45% to be the minimum
18 appropriate level.
19

20 Mr. Coyne does not recommend a common equity ratio of less than 45% and was
21 not asked to complete an analysis for returns on equity with a range of capital
22 structures.
23

- 24 c) See part (b).

³ Ibid., page 7.

⁴ Order No. P.U. 19 (2003), page 39.

⁵ See the 2022/2023 General Rate Application, Volume 1, Application, Company Evidence and Exhibits, Exhibit 4, page 5.

⁶ Order No. P.U. 18 (2016), page 24.