Q. **(Reference CA-NP-069) (Application Volume 1, pages 3-42 and 3-43) It is stated *"Mr. Coyne recommends a fair rate of return on equity for Newfoundland Power of 9.8% based upon a capital structure with a 45% common equity component."* The September 23, 2020 presentation by Fortis Inc. titled 2021-2025 Five-Year Outlook Conference Call provides the following: i) Fortis BC Electric - 9.15 ROE on 40% equity, ii) Fortis Alberta (electric) - 8.5% ROE on 37% equity, iii) Maritime Electric - 9.35% ROE on 40% equity, and iv) Fortis Ontario - 8.52% - 9.30% ROE on 40% equity.**

a) Please explain why it is appropriate for NP to have an equity component of 45% when these Canadian Fortis companies have equity components that are 40% or less.

b) What return does Mr. Coyne recommend for a capital structure with a 40% common equity component?

c) What return does Mr. Coyne recommend for a capital structure with a 37% equity component?

In response to CA-NP-069, Mr. Coyne has declined to provide his estimate of a return required if Newfoundland Power had a capital structure of (b) 40% common equity component or (c) 37% equity component.

(a) Is Mr. Coyne intending to appear as a witness on behalf of Newfoundland Power at the GRA scheduled to commence on November 23, 2021?

(b) If so, as CA-NP-069 (b) and (c) will be put to him as a question following his oath or affirmation on the witness stand, please advise if he will continue to decline to answer these questions?

(c) If he does intend to eventually answer the questions voluntarily by follow-up undertaking, following cross-examination, please provide his answers now in response to CA-NP-069.

A. (a) Yes, Mr. Coyne will appear as a witness on behalf of Newfoundland Power.

(b) Please see response to subpart (c) below.

(c) Mr. Coyne continues to believe that a 45.0% deemed equity ratio is the minimum necessary for Newfoundland Power given the business risks of the Company. As discussed on pages 7-8 of Concentric's report, there is a relationship between the equity ratio and the authorized ROE such that, all else being equal, firms with lower common equity ratios require higher rates of return to compensate shareholders for the additional financial risks. Mr. Coyne has not developed alternative ROE recommendations for equity ratios stipulated in the question. It is possible, however, to vary the equity ratio and determine a range of ROEs that would result in the same average weighted cost of capital. The approach is referred to as the ATWACC (average total weighted average cost of capital) approach to estimating these trade-offs. Please see Attachment A for those calculations assuming a reduction in Newfoundland Power's deemed common equity ratio from 45.0% to either 40.0% or 37.0%. These calculations show that the ROE would need to increase to between approximately 10.4% to 10.9% depending on the year and equity ratio to maintain the Company's weighted average cost of capital.

In addition to calculating how the required cost of equity might change depending on the Company's deemed equity ratio, it is also important to consider several other factors. First, more leverage in the capital structure (i.e., a lower deemed equity ratio) increases the financial risk of Newfoundland Power, which could result in an increase in the Company's cost of long-term debt. In addition, all of the credit metrics used by both Moody's Investors Service and Morningstar / DBRS to determine the Company's financial risk and ultimately its credit rating are affected by a change in the deemed equity ratio. Specifically, the credit metrics from Moody's and DBRS either include debt in the numerator or denominator, or are based on interest coverage ratios that depend on interest payments on debt, which are a function of the amount of debt in the capital structure.

Lastly, the Board's decision to maintain Newfoundland Power's deemed equity ratio at 45.0% for more than 20 years has been a key factor in the credit rating agencies' view of Newfoundland and Labrador as being credit supportive for regulated utilities. This has contributed to Newfoundland Power's continued access to capital markets on reasonable terms under a variety of economic and capital market conditions. A reduction in the Company's deemed equity ratio would likely be perceived by the rating agencies as a signal that the jurisdiction had become less credit supportive. The regulatory environment is an important element of the rating agencies' assessment of a regulated utility company's business risk profile, accounting for 50% of the overall rating from Moody's.

In summary, Mr. Coyne concludes that a reduction in the Company's deemed equity ratio is not appropriate for Newfoundland Power given its business risks and the value ascribed by credit rating agencies to the deemed equity ratio of 45.0% as outlined in PUB-NP-030. Such an action is likely to negatively impact analyst and investor views of the level of credit supportiveness of the regulatory environment and could result in higher debt costs for customers. For all of these reasons, Mr. Coyne continues to believe that a 45.0% equity ratio remains appropriate for Newfoundland Power.

Calculations of ROE Based on Different Common Equity Ratios

Calculations of ROE Based on Different Common Equity Ratios

As filed - 2022

		Ratio	Cost Rate	Weighted ROE
1	Equity	44.86%	9.80%	4.40%
2	Debt	55.14%	5.07%	2.80%
3	WACC			7.19%

Reduced to 40% equity

1	Equity	40.0%	**10.37%**	4.15%
2	Debt	60.0%	5.07%	3.04%
3	WACC			7.19%

Reduced to 37% equity

1	Equity	37.0%	**10.80%**	4.00%
2	Debt	63.0%	5.07%	3.19%
3	WACC			7.19%

As filed - 2023

		Ratio	Cost Rate	Weighted ROE
1	Equity	44.96%	9.80%	4.41%
2	Debt	55.04%	4.66%	2.56%
3	WACC			6.97%

Reduced to 40% equity

1	Equity	40.0%	**10.44%**	4.17%
2	Debt	60.0%	4.66%	2.80%
3	WACC			6.97%

Reduced to 37% equity

1	Equity	37.0%	**10.91%**	4.04%
2	Debt	63.0%	4.66%	2.94%
3	WACC			6.97%

Note: Source - Exhibit 5 to Newfoundland Power's GRA, Volume 1