Q. In Dr. Booth's opinion how should Newfoundland Power's credit ratings by Moody's and DBRS be considered in setting the fair return and what impact would the implementation of Dr. Booth's recommendations have, in Dr. Booth's opinion on Newfoundland Power's credit ratings?

A. Dr. Booth agrees with the BCUC (Decision G-20-12 page iii) that it is important to maintain an "A" bond rating, but that does not trump the fair return standard. The fact is that some utilities can never get a good investment grade rating due to size and risk considerations. Having said that, Dr. Booth would not put NP in that category, and both the AUC and NEB have said that they consider bond ratings when setting the common equity ratio after first evaluating business risk.

Dr. Booth is not a bond rater, but the AUC is unique in Canada in assessing the rating implications of its decisions, since it regulates a number of different types of utilities. The AUC targets an "A" bond rating, and in Schedule 13 to Dr. Booth's evidence is their schedule of the three main ratios that the bond raters use to assess credit risk. All three ratios are largely combinations of the values allowed by the regulator, that is mainly the ROE, common equity ratio and depreciation rate plus external factors such as the tax rate and embedded debt cost.

The AUC schedule is based on a 9% allowed ROE and various equity ratios ranging from 30% to 45%. With a 45% common equity ratio, the major credit metrics are almost off the table. As I explain on pages 116, if the Board had accepted my 2016 recommendation to reduce NP's allowed equity ratio to 40%, which exceeds that allowed by the AUC for T&D utilities, then the persistent decline in NP's embedded interest cost would have meant an interest coverage ratio of about 2.6, and I would have expected no change in its rating. If in addition the Board reduces the allowed ROE to 7.70%, I would expect NP would be on a ratings alert for a possible downgrade to a DBRS A(Low), similar that of other Fortis Canadian utilities.

The important criterion is a fair and reasonable ROE and common equity ratio such that the utility has a sound bond rating and can access markets to finance service to rate payers. The lowest investment grade bond rating is BBB (Low), which is four "notches" lower than NP's current rating.