1   **Volume 2: Cost of Capital: Expert Opinion of Mr. James Coyne – Return on Equity**
2
3   **Q.   Volume 2, cost of Capital Report, page 45, lines 6-7. Mr. Coyne states that the**
4   **common approach is to use Blume adjusted betas rather than raw betas. Please**
5   **provide references to all decisions in which Canadian regulators have accepted the**
6   **use of adjusted betas in the application of the Capital Asset Pricing Model in**
7   **determining a fair return for an electrical utility. Provide the same information for**
8   **U.S. regulators.**
9
10   A.   In its September 2023 Order, the British Columbia Utilities Commission ("BCUC")
11   accepted the use of Blume adjusted betas in the CAPM analysis, which were
12   recommended by both Concentric (on behalf of FortisBC Energy Inc. and FortisBC Inc.)
13   and the BCUC's consultant, Dr. Jonathan A. Lesser, who was retained by the BCUC to
14   advise it on the appropriate methodologies for estimating the cost of equity for regulated
15   utilities. Specifically, the BCUC stated:
16
17   *However, the Panel notes Mr. Coyne's explanation that Dr. Blume found*
18   *that his adjustment was applicable to all betas, ranging from a low of 0.50*
19   *to a high of 1.53, and in Mr. Coyne's view, there is no reason to expect that*
20   *regulated utilities would be an exception to this rule. Given the views of the*
21   *two experts in this proceeding and since none of the parties object to Mr.*
22   *Coyne's use of Blume-adjusted data, the Panel accepts the experts'*
23   *recommendation to use the Blume-adjusted beta estimates for the proxy*
24   *groups.*[1]
25
26   See pages 72-75 of Order G-236-23 for a discussion of the use of adjusted betas.
27
28   In addition, the Alberta Utilities Commission ("AUC") typically employs a wide range of
29   values for beta based on evidence from utility and intervenor witnesses. Adjusted betas
30   are included in this range. See, for example, the AUC's October 2023 decision, in which
31   the AUC relied on a range of betas in setting the generic ROE for Alberta's electric and
32   gas utilities. The AUC explained:
33
34   *[129]… Nevertheless, the Commission acknowledges that adjusted betas*
35   *are widely used by finance professionals, as they provide useful information*
36   *in certain circumstances.*
37   *[130] As expressed in several past decisions, the Commission remains*
38   *unpersuaded that adjusted betas are superior to raw betas in the context of*
39   *regulated utilities. Rather, it finds that both raw and adjusted betas can*
40   *provide useful information with respect to utility risk…*[2]
41
42   See pages 27-29 of Decision 27084-D02-2023 for the relevant discussion.

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[1]   See BCUC Order G-236-23, September 5, 2023, page 75.
[2]   See AUC Decision 27084-D02-2023, October 9, 2023, page 29.

In the U.S., the use of Blume adjusted betas is widely accepted. Concentric is not aware of any case where the use of Blume adjusted betas was rejected by a U.S. regulator. A recent decision by the North Carolina Utilities Commission typifies the view of U.S. regulators in accepting the standard adjusted betas as used by Concentric and other experts:

> *Modern financial theory as expressed in the CAPM posits that investors can diversify away from all company-specific risks, leaving only market risk, also known as systemic risk. Tr. vol. 7, 230; tr. vol. 14, 78. Systemic risk is represented by the symbol "beta" (β); the beta coefficient measures the change in a security's return relative to that of the market, and, therefore, measures the degree to which a particular stock shares the risk of the market as a whole. Tr. vol. 7, 230. A beta of 1.0 signifies a security that has systemic risk equal to the market as a whole. A security with a beta of greater than 1.0 signifies that it is riskier than the market as a whole, while, conversely, a security with a beta of less than 1.0 is less risky than the market as a whole. As a general proposition, utility betas have typically been less than 1.0.*

> *Securities analysts, such as Value Line or Bloomberg, calculate betas, and the use of these betas for utilities is a standard means of estimating cost of equity in utility rate cases. Each of witnesses Morin, Walters, and LaConte utilized current Value Line betas for their proxy group companies and averaged the resulting values, as follows: Morin (rebuttal testimony): 0.91; Walters: 0.88 (average) and 0.89 (median); and LaConte: 0.85.*

> *Witness Coyne notes that "current Value Line beta . . . [is] a well-regarded source investors rely on", Tr. vol. 16, 202, and witness Morin testified:*

>> *Value Line betas are widely used and well known to investors. Value Line is the largest and most widely circulated independent investment advisory service, and influences the expectations of a large number of institutional and individual investors. Value Line is a widely followed, reputable source of financial data that is frequently used by professional regulatory economists in regulatory proceedings dealing with the cost of capital.*

> *Tr. vol. 7, 362. The Commission agrees. Accordingly, for purposes of its consideration of rate of return on common equity in this case, the Commission will accept these betas as noted above, ranging from 0.85 to 0.91.[3]*

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[3] State of North Carolina Utilities Commission, Duke Energy Carolinas, Docket No. E-7, Sub 1134, Docket No. E-7, Sub 1276, December 15, 2023, at page 205.