

Volume 2: Cost of Capital: Expert Opinion of Mr. James Coyne – Return on Equity

Q. Volume 2, Cost of Capital Report, page 47, lines 21-22. Mr. Coyne recommends that an adjustment be made of 50 basis points for flotation costs and financing flexibility. In its September, 2023 decision the British Columbia Utilities Commission (BCUC) did not allow this adjustment. Please explain why Mr. Coyne believes it is not appropriate for this Board to take the same position as the BCUC did on this adjustment of 50 basis points for flotation costs and financing flexibility.

A. As discussed on page 47 of Volume 2, Concentric's *Cost of Capital* report, it is common practice for Canadian regulators to approve an adjustment for flotation costs and financing flexibility. The Board has previously determined that it is appropriate to add an allowance for flotation costs and financing flexibility of 0.50 percent to the allowed equity return.¹ This adjustment for flotation costs and financial flexibility compensates the equity holder for the costs associated with the sale of new issues of common equity, and it also provides the financial strength needed to attract capital under a variety of economic and financial market conditions.

The BCUC had previously included an adjustment of 50 basis points for flotation costs and financing flexibility in its 2016 decision for FortisBC Energy Inc. ("FEI"). In September 2023, the BCUC determined that an explicit adjustment for flotation costs had not been justified for FEI and FortisBC Inc. ("FBC"). The BCUC did, however, determine that "the Panel finds that the appropriate way to account for required financial flexibility is to adjust the utility's capital structure" and the Commission adjusted FEI's equity ratio from 38.5 to 45.0 percent and FBC's equity ratio from 40.0 to 41.0 percent.² Making the connection between equity ratio and financial flexibility for FBC, the Panel found "*In light of our decision to consider financial leverage and financial flexibility in the capital structure, we find that a modest upward adjustment in equity thickness of 1.0 percent for FBC is warranted to conform with the Fair Return Standard.*"

In addition, the BCUC set the authorized ROEs for both utilities at 9.65 percent, representing increases from 8.75 percent (FEI) and 9.15 percent (FBC) in their prior cases.

¹ In Order No. P.U. 18 (2016), the Board did not explicitly accept/reject flotation costs but did note that the CAPM results include a 50 bps adjustment.

² BCUC, Generic Cost of Capital Proceeding (Stage 1), Decision and Order G-236-23, September 5, 2023, pages 125, 134 and 135.

1 Table 1 summarizes the regulatory practice on this issue across Canada prior to the most
2 recent BCUC decision.

**Table 1:
Regulatory Practice in Canada
Flotation Costs and Financing Flexibility**

Jurisdiction	Adj.	Docket/Proceeding	Notes
Alberta	50 bps	2004 GCOC Decision 2004-052, and 2018 GCOC Decision 22570-D01-2018 27084-D02-2023	Flotation adjustment of 50 bps is normally included in the allowed return to account for administrative and equity issuance costs, any impact of underpricing a new issue, and the potential for dilution.
British Columbia	50 bps	2013 GCOC Decision Stage 1, and 2016 FEI Decision	Accepted 50 bps adjustment but cautions that the adjustment should not be considered “automatic” and instead should be considered on a case-by-case basis.
Manitoba	N/A	N/A	N/A
New Brunswick	50 bps	2010 EG Decision	Accepted 50 bps as being the lower of two proposed adjustments presented.
Nova Scotia	N/A	Not specified	The Board’s 2023 decision in Nova Scotia Power rate application did not indicate whether flotation costs were included in the authorized ROE but noted that both Mr. Coyne and Dr. Booth supported an adjustment of 50 basis points.
Ontario	50 bps	EB-2009-0084	Base ROE value included a 50 bps adjustment for flotation and financing flexibility.
Prince Edward Island	50 bps	Order UE19-08	Approved ROE included a 50 bps adjustment for flotation costs.
Saskatchewan	N/A	N/A	N/A
Quebec	30-40 bps	D-2011-182/R-3752-2011	Regie determined provision for flotation costs and other costs of accessing capital markets ranging from 30-40 bps, with a greater weighting at the lower end of the range.