Volume 2: Cost of Capital: Expert Opinion of Mr. James Coyne - Capital Structure and Risk Analysis

Q. Volume 2, Cost of Capital Report, pages 55-56, Figures 33 and 34.

a) Please re-state Figures 33 and 34 to include the date when the capital structure was last reviewed and approved by the regulator.

b) Please explain why, in Mr. Coyne's opinion, the approved common equity ratios in Figures 33 and 34 for U.S. utilities are consistently higher than for Canadian utilities and what weight the Board should give to this in setting the ROE and common equity ratio for Newfoundland Power.

A. a) Figures 33 and 34 are restated below as requested to include the date when the capital structure was last reviewed and approved.

Restated Figure 33:
Comparison of Allowed Equity Ratios and Authorized ROEs

Operating Utility	Deemed Equity Ratio	Capital Structure Review	Authorized ROE
Newfoundland Power (existing)	45.0%	2/2022	8.50%
Newfoundland Power (proposed)	45.0%		9.85%
Alberta Electric Utilities	37.0%	10/2023	9.28%
FortisBC Electric	41.0%	9/2023	9.65%
Ontario Electric Utilities	40.0%	2/2013	9.21%
Maritime Electric	40.0%	4/2023	9.35%
Nova Scotia Power	40.0%	2/2023	9.00%
Canadian Electric Average	**39.6%**		**9.30%**
US Electric Utility Average[1]	**51.6%**	Various	**9.66%**

[1] S&P Global Market Intelligence, based on electric rate case decisions from January 1, 2022 through September 25, 2023, excluding decisions in Arkansas, Florida, Indiana and Michigan where the equity ratio includes zero cost items (such as accumulated deferred income taxes) that are typically excluded from rate base in other jurisdictions.

Restated Figure 34:
U.S. T&D Utility Sample

Company	Authorized Common Equity Ratio	Capital Structure Review
The United Illuminating Company	50.0%	8/2023
Delmarva Power and Light (MD)	50.5%	12/2022
Central Maine Power	50.0%	6/2023
Versant Power	49.0%	5/2023
Orange and Rockland Utilities	48.0%	4/2022
Duke Energy Ohio	50.5%	12/2022
Dayton Power & Light Co.	53.9%	12/2022
Mean	**50.3%**	

b) The gap between allowed equity ratios for Canadian and U.S. utilities has persisted for many years. In the U.S., regulated utility companies are typically allowed to manage their ratemaking capital structure based on their actual book capital structure within a reasonable range in relation to peer companies unless the company has credit metrics under pressure or other circumstances warranting a re-examination of the capital structure. In Canada, regulators tend to deem equity ratios with a focus on the minimum necessary to maintain investment grade credit ratings. Deemed equity ratios in Canada remain lower than those in the U.S. The risk of the Canadian approach is that an unforeseen event at the utility or a disruption in the economy/financial markets may inhibit the utility's ability to raise capital on reasonable terms when needed if the equity ratio is too near the lower limit. Lower equity ratios and greater debt levels place equity investors at greater risk. U.S. utilities with higher equity ratios have less financial risk than their Canadian peers, without evidence of greater business risk, thereby offering a preferable equity investment. In Concentric's view, this has been an influential factor in the growth of investment by Canadian based utility companies in U.S. jurisdictions.

The Board should set the authorized ROE for Newfoundland Power at a level that is consistent with the fair return standard. Concentric's analysis shows that 9.85% is the appropriate return for the North American proxy group. Newfoundland Power is proposing to maintain its deemed equity ratio of 45%, which has allowed the Company to maintain its A- credit rating for many years.