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(9:00 a.m.)
CHAIR:
Q. Good morning everyone. Any preliminary matters?
MS. GLYNN:
Q. None that I'm aware of. I think we are ready to hand the baton right over to Newfoundland Hydro.
CHAIR:
Q. Good morning, Mr. Simmons.
SIMMONS, KC:
Q. Thank you very much. Good morning Chairman, Panel Members, and good morning gentlemen. As you know, I'm Dan Simmons, counsel for Newfoundland and Labrador Hydro here. I'm going to have a number of questions for you. They're fairly general, we're not going to get too deep into anything this morning, and since you're testifying as a panel, I think what I'll do is I'll generally direct the questions to you as a panel and as you've done yesterday, you can work out between yourselves who is going to speak to it or how you want to respond. If we run into any difficulty, we'll sort it out when we come

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to it. So first of all, I want to ask you about something that Mr. Coffey did ask you about yesterday which I was interested in. Early in your testimony yesterday, and Mr. Coyne it was you, who in response to a question about how your reports were prepared, that you said that "as a starting point we"--both you and Mr. Trogonoski--"go back to look at prior decisions from this Board to make sure that we haven't been tone deaf in anyway to positions the Board has taken." Now I thought an interesting choice of words, "tone deaf", I wonder if you could elaborate just a bit more on what you do to take account of decisions that the Board has made previously?
MR. COYNE:
A. Well what I mean by that is we'll look to see what pieces of our evidence and/or evidence of other experts that the Board found to be reliable for purposes of making its determination, and to the contrary, if they rejected aspects of our evidence and/or found other aspects of other witness' evidence more credible and more reliable for

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purposes, those purposes we'll look at that to see how they reached that conclusion and to see if we could approach our analysis in another way that would address any concerns that the Board would have, while staying consistent with what we think are the good principles of regulatory finance that will allow us to reach these determinations. So, as I mentioned for us, it's always a learning process and it's both a collective learning process, not just before this Board but before other boards for which we appear, and also financial markets are dynamic. They're always changing. And a case in point, as I mentioned yesterday, is our approach to the market equity risk of premium. It's not just controversial here, it's been controversial before other boards as we all wrestle what the forward looking market return is for equity markets. It's a big problem to solve in general and it's a challenging for estimating cost of capital models. So we're always just considering what the best approach to variables like that so that we can present data that we

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think will be reliable to the commissions.
SIMMONS, KC:
Q. So if I understand then, you take guidance from the Board's past decisions when you're considering what is the best data to use, what the Board would consider reliable, so you're trying to be helpful to the Board with the data you present. Do you also take guidance from how the Board in the past has interpreted your evidence and what they've done with the opinions you're presented? Do you take that as any guidance for how you might change or craft your own opinions when you come back to the Board in future hearings?
MR. COYNE:
A. We do, of course we have to stay consistent with, again, what we think are good financial and regulatory practice and there are times that a board will reach a decision that we don't understand or that we don't think was necessarily supported by the evidence. In which case we feel like we haven't done our job of presenting that evidence to the board, as well as we might,

so we don't—we try not to be dogged about it, but if we feel like we have a good point to make and we haven't made it well, we'll to approach it in a different way.

SIMMONS, KC:

Q. Sure. So it's fair to say then, there are certainly times when you may not agree with the decisions that a board, this Board or other boards have made after hearing your evidence and the evidence of others at a rate case?

MR. COYNE:

A. That does happen, yes.

SIMMONS, KC:

Q. Would it be fair to say here that you haven't agreed with the outcome of the last couple of GRAs which has been a return on equity of 8.5 percent for Newfoundland Power?

MR. COYNE:

A. No, that's not true because the last two were both settled cases and in our view when parties, and we like to see it when parties do settle, there is a balance of interest that is achieved and we think that the

company and parties that come to the table and can balance their own interest, I think that serves as a good practice and I think that's one that's helpful to boards like this, knowing that that balance has already been struck.

SIMMONS, KC:

Q. Would you agree with me then, that while a settlement is useful and that, as you say the parties balance their interests, perhaps to come to some compromise, if they fail to do so, the job then falls to the board to conduct that balancing of interests.

MR. COYNE:

A. That's right.

SIMMONS, KC:

Q. My first pen has failed already, it's a bad sign for this morning.

MR. COYNE:

A. I have an extra if you need one.

SIMMONS, KC:

Q. Okay, I'm good, thank you. So can we go, please, to the Concentric Report. It's found, as I expect you know at Volume 2 of Newfoundland Power's submission. I'm going

to go to page 33 of the report which I think is pdf 143. And this is not a controversial point. If we go to the bottom of that page –

MS. BOWN:

Q. Do you have the page number? Sorry.

SIMMONS, KC:

Q. It should be page, of the pdf page 143, which should be page 33 of the report, unless I've calculated that incorrectly. That's it there. So in this section which is addressing methods for estimating the cost of equity, you've made a comment in line 26 and 26 there, "No financial model can exactly pinpoint the correct ROE, rather each test brings its own perspective and set of inputs that form the evidence." So another very general question for you, gentlemen, how much is this setting of a return on equity art and how much is it science? How much is it just working the numbers and doing the math and how much of it is the experience and judgment that has to be brought to bear by people knowledgeable of the art of setting an ROE?

MR. COYNE:

A. Hmm, what a terrific question. Oddly enough, never been asked it before. May even have different perspectives on this, but the models themselves are pretty tried and true. There's not—some experts might put a different amount of weight on the CAPM versus DCF or the risk premium which are the three that we primarily use, but most experts use a combination of at least two of those, if not three of those. So there's pretty little controversy there. Those are well established. The judgment comes in the section of the inputs and our view is that while we may be experts in these areas, the less we substitute our own judgment for market data or data that we can take from other reputable sources, the less controversial that is and after all, we're trying to determine the market based rate of return on equity ultimately. So I would say that in our choice of inputs to the models, we by and large rely on external sources, such as Bloomberg and Value Line, Zacks, et cetera, that project earnings growth rates.

CAPM we're deriving from historic market data. Forecast for the risk free rate we take from Consensus Economics. So I can't think of any input to the models that we're using where we're substituting our judgment to say that we think, for example, beta should be this. We're measuring beta through Bloomberg or Value Line sources. So I would say that we try to minimize the judgmental elements of it by using data inputs that come from these reputable third party sources, but at the end of the day, you can take, use inputs from multiple sources. Where that's the case, we try to take it from multiple sources and we may average them so that we get the benefit of a perspective from the market. That being said, if you're solving for three different models, you'll get a range and oftentimes we take the midpoint of that range to try and find a center point of the evidence, so again try to minimize the judgment and let the models and the market data do what they do best, and that is inform us as to what the required return is. So there is some

combination of that, I couldn't give you an exact percent, but I would say the less art and the more science, the more reliable the estimate in our view.

SIMMONS, KC:

Q. So would there be an element of judgment involved in selecting which models to use, how to weight them, for example?

MR. COYNE:

A. Yes.

SIMMONS, KC:

Q. And there's an element of judgment in selecting the input data that goes into the models?

MR. COYNE:

A. Yes.

SIMMONS, KC:

Q. And once you have the model results, there's another layer of judgment that overlays that then in how you interpret the different results from the different models and apply them to the case that's before you, is there?

MR. COYNE:

A. Yes.

SIMMONS, KC:

Q. And then ultimately the last element of judgment will be how the board members take your evidence and apply their own experience to it to make their determination.

MR. COYNE:

A. Perfectly described. And I didn't let Mr. Trogonoski answer, but he may have a different sent of answers around the art and science question which I thought was important.

(9:15 a.m.)

MR. TROGONOSKI:

A. No, I really don't. I think one thing Mr. Coyne did not mention though is how we use the economic and capital market data as context for the results of the models, so I think it's important also to consider what's happening with interest rates, what's happening with inflation, the trend in both of those and that kind of tells us what to expect in the future and the kind of returns investors might be requiring for a company like Newfoundland Power, so I think that also helps to inform the judgment piece of

what we do here.

SIMMONS, KC:

Q. Okay, thank you. And I have a couple of more specific questions now on the results of the models, the DCF model, the CAPM results which I'm not going to get very deeply into Can we go to page 41 of the report please? Pdf 151. Okay, you can stop there. So it's Figure 24 I think presents the results of your calculations from your DCF model, is that correct?

MR. COYNE:

A. That's right.

SIMMONS, KC:

Q. And it is a very straightforward question these percentage numbers here, these are, if I understand correctly, return on equity, ROE rates, without taking any account of the relative capital thickness of the companies that apprise each proxy group, do I have that right?

MR. COYNE:

A. I wouldn't say without taking into account, they're based on a proxy group that has a given capital ratio and the market data says something about that equity ratio, but we haven't made any adjustments for the average equity ratios of this group, so it's coming straight out of the models, given the equity ratios these companies already have, and you can say that those equity ratios might have some impact on the market data that's determining the return is filtering through the model. Some analysts will make an adjustment for differences between the target company's equity ratio and the average for the proxy group, but we haven't done that. If you take a look at the average equity ratios for this proxy group, it's on the order of just over 50 percent.

MR. TROGONOSKI:

A. 50 percent, 51 percent.

MR. COYNE:

A. And the average equity ratio for Newfoundland Power is 45 percent. If we were to apply an adjustment, we would increase the ROE coming out of the models because Newfoundland Power has a lower equity ratio than the average of the proxy group companies, but we haven't made that

adjustment.

SIMMONS, KC.:

Q. So the models themselves, if we went back to the formulas of the calculations that make up the models, the equity ratio of each company isn't a factor in those formulas, it's not an expressed piece of the calculation that goes into it.

MR. COYNE:

A. No, you have to make an adjustment after the fact for the difference between your target company, Newfoundland Power, and the average for the proxy group if you're going to do that.

SIMMONS, KC:

Q. And if I understand what you've said, the underlying data, that market data that you used to plug into those models, may indirectly have already taken account of the equity ratio when the analysts had prepared that data?

MR. COYNE:

A. That's right.

SIMMONS, KC:

Q. Did I understand you to say that?

MR. COYNE:

A. Yeah, that's right. The way this gets done if you want to make an adjustment, is to use something called the Hamada Equation, is when we approach that where you decompose your proxy group for its proxy group, and then you re-examine those results for the target company's actual equity ratio. And in this case, because Newfoundland Power has a lower equity ratio than the proxy group, the net effect would be to increase, you see the average, for example here of 9.7 percent for the North American electric utility group, actually we've relied on the multi-stage version of it which is 9.42 percent. I don't have the precise number here, but if we were to adjust that for Newfoundland Power, that number would probably over 10 percent because there's a 5 percent difference in the equity ratio for Newfoundland Power versus the proxy group and we haven't done that.

SIMMONS, KC:

Q. Right, so you haven't done those calculations and presented them here.

MR. COYNE:

A. No.

SIMMONS, KC:

Q. No, okay.

MR. COYNE:

A. So the net increase would be to—the net impact would be to increase the ROE which we have not taken into account.

SIMMONS, KC:

Q. And if we were to look at your CAPM calculations, would it essentially be the same answer, the ROE is not the—the equity level is not explicitly taken into account in the calculations that are done for the CAPM figures?

MR. COYNE:

A. No, the same, we've accepted those equity ratios as being representative of Newfoundland Power, the results coming out of those models as being representative of Newfoundland Power without making any upward adjustment.

SIMMONS, KC:

Q. Can we go to page 55 please? And scroll down to Figure 33 and you can stop there.

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And we may have looked—you may have been brought to this before, I'm not sure, in the previous examination, but I understand this to be a table that compares the common equity ratio of the listed companies or averages, and also lists their authorized return on investment and these are actual numbers for the companies that are listed there, correct?

MR. COYNE:

A. They are, they've since been updated and we provided an update to that in our rebuttal evidence, but the table accomplishes the same thing. I think the only thing that changed was the Alberta number changed between when we filed our direct and rebuttal.

SIMMONS, KC:

Q. Okay, well aside from that, if it's okay with you, I'll use this table just to ask you a couple of questions about it.

MR. COYNE:

A. Yes.

SIMMONS, KC:

Q. And I know in your rebuttal evidence you

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also included a very helpful bar graph which you were brought to yesterday, which presented weighted, the weighted return on equity, and I've made some assumptions here, so I'll just through this with you from this table. If, for example, we were to look at Newfoundland Power's existing weighted return on equity, we would multiply the 45 percent by the 8.5 percent?

MR. COYNE:

A. Precisely.

SIMMONS, KC:

Q. Correct, okay. So the first question is that seems to be a very useful measure and is that something that's common or standard in your analysis to prepare and present that kind of weighted equity data?

MR. COYNE:

A. Increasing so, especially where we see the differences between ROEs or equity ratios and you don't get the combined effect until you look at what the rate effect is going to be and you do that by multiplying them and that shows the, in our view, that shows a balance perspective on the overall risk and

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return to the equity investor, and John, I think in most of our Canadian evidence we have a table like that for that purpose. Not always in our US evidence because oftentimes the peer groups are more aligned from an equity ratio than they are in Canada.

SIMMONS, KC:

Q. Okay, interesting. And are there different ways to do the weighting, or is this the accepted approach just to take the equity ratio and multiply it by the return on investment?

MR. COYNE:

A. I don't know of any other approach you could take because from a rate perspective, that's how these flow through rates, you know, you compute a weighted average cost of capital which is the common equity ratio times the allowed ROW and the debt portion of the capital structure times the weighted average cost of debt. You add those two together and that is the cost of capital that flows through rates. So I can't think of any other way to do it.

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SIMMONS, KC:

Q. Would it be fair for me to suggest that using the weighted cost of capital is a good way to assess what the value to the shareholder is of the company because it takes account of how many shares are issued, how much income there's going to be and is therefore, a good proxy for assessing what the likely dividend return is going to be for that shareholder.

MR. COYNE:

A. I wouldn't go that far. I think from a shareholder perspective the dividend return is going to take into account, as you said, the number of shares outstanding times the return per share. So they wouldn't go through this calculation to make that determination specifically.

SIMMONS, KC:

Q. But you could see there being a correlation, a connection between the two. The higher the weighted return on equity, the higher the relative return to the shareholder is going to be.

MR. COYNE:

A. I would say the higher the absent return would be, as opposed to relative.
SIMMONS, KC:
Q. Okay, all right, thank you. Now, this is your originally filed evidence and it includes the, I'll say the raw data here for the equity ratio and the return on equity, but you haven't included a weighting calculation in your original evidence like you did in your rebuttal. Is there any reason why you didn't present that as part of your evidence here?
MR. COYNE:
A. Well at this point in time we're just trying to do a build up of the recommendation, it's not a comparison against other recommendations. When we get to the rebuttal evidence, we had a recommendation from Dr. Booth that we wanted to put in perspective with regards to other allowed returns and our recommended return, so in that sense, we thought it was a more useful way of presenting the data than it is in the direct evidence. There, it's more of a ground-up analysis.

SIMMONS, KC:
Q. So you'll have to bear with me now, we're going to do a little bit of math, which I expect both of your gentlemen are pretty good at. So if we were to look at the Canadian average here, which is the deemed equity ratio of 39.6 percent and the authorized return on equity of 9.17 percent, if we multiply those two together, I get 3.63, does that seem correct to you?
MR. COYNE:
A. Well we can do the math, but why don't we accept that subject to check.
SIMMONS, KC:
Q. Okay, I've tried to do it a couple of times, I stand to be corrected, but I get 3.63 for that –
MR. COYNE:
A. It looks about right, yeah.
SIMMONS, KC:
Q. And if we look at Newfoundland Power's existing numbers, if we multiply 45 percent by 8.5 percent, I get 3.825, so it's essentially .2 higher than the Canadian average, does that sound correct?

MR. COYNE:
A. We've done that for you on page 39 of our rebuttal evidence, except we're not doing the Canadian average there.
SIMMONS, KC:
Q. Right, the Canadian average is not included in your chart, which is why I'm asking here now.
MR. COYNE:
A. I see, yeah. So we have 3.83 there for Newfoundland Power, so I can confirm that, yeah.
SIMMONS, KC:
Q. So the conclusion I can draw from that is based on these current numbers, and subject to some adjustment to the Canadian average for the Alberta number which you said you've updated, the current Newfoundland Power weighted average return on equity is above the Canadian average?
MR. COYNE:
A. Well let's, again, the Alberta number has come up and that would probably move it closer to the average.
SIMMONS, KC:

Q. Right.
MR. COYNE:
A. I could do that math, but –
SIMMONS, KC:
Q. So, I mean, we can do that, but now –
MR. COYNE:
A. But I accept the principle that they would probably be close. But I think if you looked down below to the US average, of course, you can see that that number is going to be substantially higher.
SIMMONS, KC:
Q. Right, and this is my next question for you, if you do the same thing for the US average, I'm getting almost 5, 4.98 as being the number I get compared to the Canadian average, which on this table is calculated at 3.6, so it appears the US average is considerably higher than the Canadian average here, would that be correct?
MR. COYNE:
A. That's right, yeah, and a lot of that has to do with the equity ratio that's so much higher than the Canadian average.
SIMMONS, KC:

Q. Now, I gather the position you've taken in your analysis is that the US data, much of the US data is as good a comparator for Newfoundland Power as the Canadian data is, but my question here is do we have any explanation as to why this US utility average of weighted return on equity is so much higher than the Canadian average, and I'll just jump in, it strikes maybe there's three—I'll present three alternatives and you can tell me if either of those make sense or explain whatever you think the reason is. One is that the Canadian average is just too low and boards all need to raise it. The other is the American average is too high and regulators need to lower it. A third is that market forces being recognized by the boards are signaling that there's less risk in Canada and that's why the weighted averages are lower. So I'd welcome your response to those alternatives and how else you would explain it?

(9:30 a.m.)

MR. COYNE:

A. Those are the only three answers.

SIMMONS, KC:

Q. Sorry?

MR. COYNE:

A. I was asking are those the only three answers, I assume, yeah. If you look at—maybe we'll just start by looking at the authorized ROEs. In Canada there's been a journey over the last two decades witnessed of ROEs that largely were based on formulas. They were a really good idea when they were initially set, they were tied to government bond yields as they were here in Newfoundland and then we entered this period of basically a two decade, tremendous period of low inflation and progressively lower interest rates and as a result of that, government bond yields followed suit and declined over the course of that approximate 20 year period. And as a result of that, ROEs in Canada and the US that used to be closely aligned, I think there's a chart in one of the IRs to that effect, separated and separated significantly, and one at a time, Canadian jurisdictions reconsidered the matter of using a formula and those ROEs

that were growing increasingly low as a result of that, separated from, in your view, what a fair return would be, and by and large beginning with the NEB in each jurisdiction that had used a formula, suspended or as was done here, set aside the formulated approached. But there was a gap that was created in that period of time and since then, it probably reached its maximum around 2008 or '9 and since then, it's been closing as each Canadian jurisdiction has reconsidered market evidence and in the case most recently in Alberta and BC, for example, recognizing that markets are integrated and the industries are integrated and it's appropriate to consider both North America and US data, and as a result of that, the gap has closed. You can see here that the Canadian average of 9.17 versus the US of 9.66 is about a 50 basis point differential. That differential was about 200 basis points back around 2007, '8 and '9 when this problem was, I think, at its greatest. So that's the ROE story, but I now see more of an integrated approach in

Canada that looks more like it does in the US, looking at market data as a basis for determining returns, as opposed to a formula that frankly just wasn't working. There's a different story on the deemed equity ratio side. In Canada we have seen a focus on setting ROEs that were targeted towards maintaining a minimum credit rating with largely a focus on debt investors and maintaining a minimum credit rating; whereas, in the US we have seen a focus on a few different dimensions, a credit rating being one aspect of that, peer group equity ratios being another aspect of that, a business risk analysis around the utility and also a little bit more—and a reflection of the actual capital structures that were being maintained by the utilities because using those actual capital structures, they were raising debt and that debt cost is impacted by the actual structure of the utility. So I would say it's been a more comprehensive approach of examining capital structure in the US in that regard than there has been in Canada, with a focus, fairly narrow focus on maintaining a minimum credit rating and as a result of that, we see this different that prevails of substantially lower equity ratios. There has been some change in some jurisdictions in Canada around that issue, the most recently in BC we saw a significant movement in equity ratios acknowledging these differences and also acknowledging the shifts in business risk for utilities, so as a result of that, the BC commission moved up the gas utilities equity ratio to 45 percent which was a significant move over where it was previously, but the electric utility up to 41. So I think it's not yet an integrated approach that we see on the equity ratio side, as we have seen happening on the ROE side. I think it's still a piece of work in motion, as I see it, as regulatory bodies consider this evidence.

SIMMONS, KC:

Q. So if I could try to summarize what you just said and I appreciate the answer, it sounds to me like your view is it's the Canadian regulators that need to change, not the

American regulators?

MR. COYNE:

A. That's really not what I said, I'm just saying that the Canadian regulators have viewed this evidence differently than American regulators have, with a different focus on the equity ratio. I see more homogeneity on the ROE side today than I do see on the equity ratio side, but I think that's also an evolving view of the world in Canada. I don't see change in the US, but I do see an evolving view of the world in Canada in that regard.

SIMMONS, KC.:

Q. Okay, and it's not your view that the US utility, electric utility average weighted return on equity is too high, it's your view that the Canadian average is too low?

MR. COYNE:

A. No, well if you look at our recommendation, you know, we have now recommended a US electric utility average equity ratio for Newfoundland Power. Our recommendation strikes a balance between the Canadian view of the world and the US view of the world,

and also we have spent some time interviewing equity rating analysts and also credit rating agencies on these issues as we have tried to understand their different approaches to rating US utilities and Canadian utilities. We've spent quite a bit of time with Moody's and S&P on this issue, interviewing their credit rating analysts. We hired the S&P senior credit rating analyst to our team to give us greater depth of knowledge around these issues, and what we've learned in that process is that the rating agencies used to maintain different offices in Toronto and in New York for rating Canadian versus US utilities and have now taken a more global approach so that they have one team, and they are conducting the ratings for both, not only just Canadian and US utilities, but also for European utilities and utilities overseas, so they're not starting to see the world through one lens around business risk, country risk and things of that nature. So as capital markets have become more integrated, the approach of investors and credit rating

agencies has now become more integrated. So I see it as, well, that's probably a longer answer than you wanted, but that's where we're coming from.

SIMMONS, KC:

Q. So just to close out this discussion then, we'll take a look, please, at the Rebuttal Report and at Figure 1 which is on page 10 of the Rebuttal Report, I think it might be pdf page 70 of the evidence. Yes, you've got it, look at that. Okay, right there. So we just done the calculation of the Canadian average before the Alberta adjustment and looking at the scale on the left-hand side of the chart, if we were to slot 3.6 in there somewhere, it's going to be somewhere to the left of the Newfoundland Power grey bar which is the current weighted average for Newfoundland Power, so it's going to slot in some distance to the left of that, isn't it?

MR. COYNE:

A. Well, if you're to use 3.6, why don't we compute the actual number.

SIMMONS, KC:

Q. Sure, if you want to do that, sure.
MR. COYNE:
A. Well actually, I want to say we should at least include the updated Alberta number if we're going to use that number for this discussion.
SIMMONS, KC:
Q. Okay, all right, if that can be done quickly, fine, if not, maybe what I'll do is just ask you for an undertaking to provide that number afterwards.
MR. TROGONOSKI:
A. Why don't we do an undertaking.
SIMMONS, KC:
Q. Okay, that will work, thank you.
MS. GLYNN:
Q. So that would be undertaking No. 6 is to provide the updated Canadian –
SIMMONS, KC:
Q. Weighted, yeah –
MS. GLYNN:
Q. Average for the rate of cost of capital.
SIMMONS, KC:
Q. Right, Canadian average.
MR. COYNE:

A. So with that stipulation we can proceed.
SIMMONS, KC:
Q. Okay, yeah. Okay, can we go back, please, to the original report, page 69 of the report please. The bottom of the page, and this point has probably been already made, I just want to confirm it, at line 27, 28 there in talking about your conclusions on business risk for Newfoundland Power, you said, "Historical risks have continued to persist and the business risk for Newfoundland Power is comparable to that in 2021 or the company's previous GRA filing." Now in your evidence yesterday I did hear you to say that you regard Newfoundland Power's business risk to be higher than other Canadian utilities or the average Canadian utility, which I understand your evidence on that, but even though it's higher than the Canadian utility, it's no different than it was at the last GRA, right?
MR. COYNE:
A. That's right. We didn't see any fundamental change from that GRA to this one.

SIMMONS, KC:
Q. And would it be fair to say that from between one GRA and another the characteristics of some of the risks might have changed, but your overall assessment is that the overall business risk is unchanged.
MR. COYNE:
A. That's right.
SIMMONS, KC:
Q. And if we were to look back at the previous two GRA applications by Newfoundland Power, do I recall correctly that your view then was that there was not any material change in the overall business risk of Newfoundland Power on either of those occasions either?
MR. COYNE:
A. I think that is correct, let me just test my memory with Mr. Trogonoski's here.
MR. TROGONOSKI:
A. Yes, I would agree with that as well.
SIMMONS, KC:
Q. Okay, so since 2016 then, characteristics of the risk may have changed, it's basically the same, I presume through all that period you would have said it's higher risk than

other Canadian utilities, as you say at this hearing.
MR. COYNE:
A. I believe that's, yeah.
SIMMONS, KC:
Q. So if the only factor that had to be considered here in setting the return on equity for Newfoundland Power at this hearing was its business risk, would there be any reason for the Board to treat it any differently than they did at the last three hearings when they set it at 8.5 percent? If that were the only factor, hypothetical, I know, and I know there's other factors but I'm just teasing this one out.
MR. COYNE:
A. I think that would be off the mark if you're talking about setting—well, maybe, are you referring to ROE or equity ratio when you ask that question.
SIMMONS, KC:
Q. ROE.
MR. COYNE:
A. Yeah, well business risk is captured in the market models when we estimate ROE, so when

we estimate the DCF model or the CAPM model or the Risk Premium Model, the market data that we discussed in your opening questions is all captured by that market data. So as business risk changes in the industry when we run these market base models, the inputs to the models are capturing those changes in business risk, so that's why a model that we would have run in 2016 would give us a different set of results than it will in 2024 because of changes in capital markets, you know, investors consider business risks when they value the stocks of these companies, they also consider macro economics, inflation, risk free rates, they're alternative investments, so to answer this Board would, I think, would not be well informed if it were only looking at changes in business risk between 2016 and 2024 when it came to determining ROE because it would not be considering all the other aspects that go into the value of a security and those change considerably over time.

SIMMONS, KC:

Q. So is your answer then that you can't answer

my question because you can't really tease out the business risk from the other factors in the way I've asked you to do?

MR. COYNE:

A. Can you restate, if you would, how you're asking me to consider –

SIMMONS, KC:

Q. I had asked you if you could just imagine that the only factor was the business risk and there's no change in Newfoundland Power's business risk over that overall period of time, so there would seem to be no reason to change the return on equity over that period of time if that were the only factor, and I asked you if that was the case. And what I take what you've told me is that it's hard to do that because you also have to take account of other changes in the markets that investors look at.

MR. COYNE:

A. Well, yeah, my simple answer is no and the reason my answer is no is because you would be ignoring all the other data that goes into determining a proper return and much more goes into it than just a simple

examination of business risk.

SIMMONS, KC:

Q. Okay, I have a more specific question for you now. Can we go to page 44 of the report please? This is one question concerning the CAPM inputs and just scroll down to Figure 27, you can stop there. So I don't pretend to fully understand what the beta is and how it all works, other than I know it's an input into the CAPM and it's got something to do with risk and I understand, and correct me if I'm wrong, that Value Line is a service that does calculations of beta values that are available to be used in situations like these calculations, right?

MR. COYNE:

A. Yes.

SIMMONS, KC:

Q. And they are the source for these three beta numbers, for the Canadian group, the US electric utility group and the North American electric group. The Canadian number looks to be materially lower than the US number and the North American aggregate number and my question is, is that an

indication that the markets from which these data were drawn by Value Line, are valuing the Canadian group as less risky than the US group and the North American group?

MR. COYNE:

A. Let me just turn to the exhibit, I just want to make sure we have the same coverage as we did for the US companies. Sometimes there are coverage differences before I answer your question more generally.

SIMMONS, KC:

Q. Yes, whatever you need to do to answer the questions, okay.

MR. COYNE:

A. Yeah, so in response to a request, actually one of your data requests –

SIMMONS, KC:

Q. Which one?

MR. COYNE:

A. This is NLH-NP-142, we addressed this issue and the question was asked, just as you asked it now, and the problem there is that Value Line only covers two of the six companies in the Canadian proxy group, Amera and Embridge, and so to make a comparison of

Value Line versus the US companies when you only have two, I think is probably fraught with peril, so that's why we also look at Bloomberg and you can see there where we do, we have estimates for all six companies, you can see that they're much more closely aligned. So I wouldn't reach the conclusion that you've suggested based on those two companies alone.

SIMMONS, KC:
Q. But nevertheless you did include the data here in your report.

MR. COYNE:
A. We did, yeah, and we relied on in our estimates.

SIMMONS, KC:
Q. Uh-hm.

MR. COYNE:
A. But at the end of the day the Canadian numbers coming out of our models were higher than the North American proxy group that is the base of our recommendation.

SIMMONS, KC:
Q. Okay, so how you assess what data to use here, that kind of circles right back to one

of my earlier questions about bringing judgment to bear about what the input data is into all these calculations.

MR. COYNE:
A. It is and that's why we use three different proxy groups, Canadian, US and North American and we looked at the composition of the companies in those proxy groups, as well as the market inputs we were using and felt as though the North American proxy group was the most representative for the purposes of this determination. And we also, when you do—the problem you pointed out, we've identified together of two companies in our Canadian proxy group is a challenge and when you have 14 companies, such as we have in the North American proxy group, then you don't have to be as concerned with your lack of good market data.

SIMMONS, KC:
Q. Just one other question for you on the risk topic and then we're getting close to the end here. Can we pop up NLH-NP-133 please? Newfoundland Power, of course, raises money by borrowing as well, by issuing debentures

under a trust deed, and the response to this RFI, we said that the long-term first mortgage bonds are typically purchased by a small number of investors, which could vary, and the primary investors in the company's first mortgage bonds are located within Canada. So, there's an indication here that – and of course, Newfoundland Power doesn't issue shares directly, so it doesn't directly participate in equity markets, so we don't have, you know, hard data about who the investors would be in Newfoundland Power, but we do have hard data here for debt placements, that the investors are Canadian and they're not American.

MR. COYNE:
A. Um-hm.

SIMMONS, KC:
Q. So, is this an indication that we should be taking into account to say that the competitive market for who the investors might be in equities for Newfoundland Power would probably also be Canadian?

MR. COYNE:
A. I wouldn't reach that conclusion.

Newfoundland Power is a very small utility, as we discussed yesterday, and so, therefore is limited to tapping into this private placement market, and its robust enough for a company that's raising relatively small amounts of capital to tap into those markets. But on the equity side, it's a different – oh, good, you found what I was thinking about. If you turn to page – if you turn to PUB-NP-115, I think it provides the comparison that would – the companion comparison on the equity side which we should be focused on here as well. And is it possible to bring that up?

SIMMONS, KC:
Q. That's up there now, yeah.

MR. COYNE:
A. Okay, and if you could scroll down to Table 1? Right. So, there you could see the parent company, Fortis Inc., of Newfoundland Power is raising 50 percent of its equity in Canada and 26 percent in the US and 17 percent in other countries, and you can see that this is true for all the Canadian companies that they're – and this is the

very premise of our view that it is an integrated North American market for capital for utilities and other companies when you can see how these companies go in the market. Canada is a portion of it, but US is an important portion or source of equity capital, along with other countries.

SIMMONS, KC:
Q. Does Fortis have subsidiary operations in the United States as well?
MR. COYNE:
A. Oh yes.
SIMMONS, KC:
Q. I see Hydro One is predominantly Canadian institutional investors. Does Hydro One have any operations outside Canada?
MR. COYNE:
A. No, but yet they're still raising capital outside Canada.
SIMMONS, KC:
Q. Yeah, 21 percent of their capital.
MR. COYNE:
A. Right.
SIMMONS, KC:
Q. 79 percent is within Canada.

MR. COYNE:
A. And this is for a company that's exclusively an Ontario company.
SIMMONS, KC:
Q. Right.
MR. COYNE:
A. And the reason for that is that, you know, you want to take advantage of the most competitive markets you can for attracting capital, and if you can shave a basis point off, here or there, attracting equity, equity capital, then you do. And that's why these companies have taken the time and expense to list in both Canada and the US.
SIMMONS, KC:
Q. I had a couple clarification points kind of for the record related to the recent rate mitigation announcements, and one really is just a correction for the record. In the – I'll make the reference to the transcript from yesterday. I don't know if we need to go to it. I'll – it's at page 55, lines 3 to 10. But I'll just tell you. Mr. Coffey asked you a question and his question asked you whether rate mitigation that's been

announced cap increases in rates charged by Hydro to Newfoundland Power at 2.25 percent. I think he probably meant to say that the rate mitigation was going to cap the increase in consumer rates related to Muskrat Falls by 2.25 percent. Does that sound correct? I think Mr. Coffey is nodding on that one.
COFFEY, KC:
Q. Yeah.
SIMMONS, KC:
Q. Because you agreed with his question on it, and I just want to make sure that you understood that the 2.25 percent is the Muskrat Falls effect on consumer rates that's being capped. Is that what you had understood?
MR. COYNE:
A. My – I've had to check my own thoughts on this and I believe, and again, and I would defer to the other experts at the company who know this better than I do, but my understanding is that the 2.25 percent is a cap on Hydro's rates that it would charge to Newfoundland Power for Muskrat Falls. So,

that's my understanding.
SIMMONS, KC:
Q. Okay, fine, but so, I know you'd been questioned on a couple press releases that have been put in evidence here. So, in preparation for coming here and testifying over the last couple days, did you do anything to familiarize yourself with any of the details of the recently announced rate mitigation plan?
MR. COYNE:
A. I looked at the press release, or I'd say we looked at the press release and we looked at the slide deck that came along with it.
SIMMONS, KC:
Q. Yes, okay, all right. And coming out of that, your understanding is the 2.25 percent is a cap on Hydro's charges to Newfoundland Power?
MR. COYNE:
A. That is my understanding. But let me just check with Mr. Trogonoski.
SIMMONS, KC:
Q. That's fine.
MR. COYNE:

A. Do you agree? This could be our disagreement.
SIMMONS, KC:
Q. So, maybe I could help with this. Maybe we can bring up Information Item No. 7 please, which is the – one of the press releases, and we'll go to page five, and scroll down to the next paragraph. You can stop there. I'm looking at the paragraph that begins "the majority of residents pay Island Interconnected fees" and if you go to starting there on the second sentence. "Each year we apply to the Public Utilities Board, the regulator, to update the rate we charge to Newfoundland Power. That rate will now be set to ensure that Hydro's impact on customer rates is limited to 2.25 percent." See that?
MR. COYNE:
A. I do.
SIMMONS, KC:
Q. Okay.
MR. COYNE:
A. I think that's consistent with my understanding, although I think the sentence

could – maybe there's some ambiguity in the sentence, also from my perspective. The way I read that and interpret it is that the rates that Hydro charges to Newfoundland Power will not go up by more than 2.25 percent as a result of the Muskrat Falls Project. That's what I take away from that.
SIMMONS, KC:
Q. Okay. Well, we'll leave that there, and while we're here on this, can we go back to page four, please? You can stop there. Now, one of the things you'd said yesterday was that you'd regard the rate mitigation arrangements which extend out to 2030 as being, I think you described it as a stop-gap measure and you described it as kicking the problem down the road, and I do understand what you're saying that right now, we don't know what will happen in 2030. We don't know if there will be further rate mitigation or what form it will take or what circumstances will have changed. So, rate mitigation buys certainty till 2030, but there's still uncertainty after that. So, that's part of what you'd said yesterday, I

think, right?
MR. COYNE:
A. I think that's a fair characterization.
SIMMONS, KC:
Q. Right. And the point I want to confirm with you is if you look at this section of the press release that says, "who is paying for Muskrat Falls and how much?", it says, "the exact sources and amounts of funding may vary each year, but essentially, the difference will be funded by Hydro. Beyond the amount recovered from customers and from Federal funding sources, between now and 2030, Hydro will invest more than two billion to mitigate customer rates." Now, I don't know how much you know about the mechanics of how this financing works at Muskrat Falls, but when you said that the problem was being kicked down the road, did you intend to say that any of the payment on the Project that had to be made up to 2030 was being postponed until after 2030?
MR. COYNE:
A. Not any. The press release indicates that a small – as I recall, a small amount of the

Project, only – I think it states only a small amount of the Project will be recovered during this period.
SIMMONS, KC:
Q. Will be recovered from ratepayers.
MR. COYNE:
A. Recovered from ratepayers, yes.
SIMMONS, KC:
Q. Right. And as -
MR. COYNE:
A. My understanding is that what is not recovered from ratepayers -
SIMMONS, KC:
Q. Yes.
MR. COYNE:
A. - will be in a deferral on Hydro's balance sheet.
SIMMONS, KC:
Q. Oh.
MR. COYNE:
A. And how that is going to be recovered in the future remains to be seen.
SIMMONS, KC:
Q. Um, and what's the basis of you thinking that it's going to be all deferred?

(10:00 a.m.)
MR. COYNE:
A. From my reading of these press releases and the slide deck, that was the conclusion that I reached.
SIMMONS, KC:
Q. So, do you know what this reference here to Hydro investing more than two billion to mitigate customer rates is about?
MR. COYNE:
A. I don't know. It has no more clarity to it than that.
SIMMONS, KC:
Q. Okay, all right. Okay.
MR. COYNE:
A. If Hydro is investing, it could be investing in maintaining that deferral is one of the ways one could interpret that.
SIMMONS, KC:
Q. Great. Thank you very much. I don't have any other questions.
CHAIRMAN:
Q. Thank you. Over to Ms. Greene.
MR. JAMES COYNE AND MR. JOHN TROGONOSKI, CROSS-EXAMINATION BY MAUREEN GREENE, KC

GREENE, KC:
Q. Thank you, Mr. Chair, Commissioners. Good morning.
MR. TROGONOSKI:
A. Good morning.
GREENE, KC:
Q. In your report, Attachment 1 outlined a number of the regulatory proceedings in which you have been an expert and similarly -- actually for Mr. Coyne and for Mr. Trogonoski, and I believe Mr. Coffey also asked you questions with respect to your experience. In the – I think you had indicated you appeared in about 20 proceedings in Canada. Is that correct?
MR. COYNE:
A. That sounds about right.
GREENE, KC:
Q. And in those 20 proceedings, on whose behalf would you have provided expert opinions?
MR. COYNE:
A. The vast majority of them would have been on behalf of utilities. I think the one exception I can think of would be in the work that we did for the Ontario Energy

Board back in 2007 or '08 when we prepared an expert report for the Board, helping them understand the differences between allowed returns in Canada and the US and that became an expert report of the Board on that issue.
GREENE, KC:
Q. And would your response be similar for your regulatory work in the United States?
MR. COYNE:
A. I would say the vast majority are for utility companies or pipelines or electric transmission companies, although we sometime – and I have sometimes also appeared on behalf of industrial consumers as well.
GREENE, KC:
Q. Mr. Trogonoski, in your experience as an expert, providing expert opinion, for your testimony, who would your client primarily have been?
MR. TROGONOSKI:
A. In Canada, it would primarily have been for the regulated utility companies, but I also have experience, as I said yesterday, as a staff member with the Colorado Public Utilities Commission. So, there, my

recommendations were on behalf of Commission staff. So, I think if you look at my listing of expert testimony, probably about evenly divided between utility clients and staff recommendations.
GREENE, KC:
Q. But in your role as a consultant, you have primarily acted for utilities? Is that correct?
MR. TROGONOSKI:
A. Yes, with the exception of what Mr. Coyne just mentioned, our work for Ontario in 2007 and 2008.
GREENE, KC:
Q. And I believe as well yesterday, Mr. Coyne, you indicated in response to a question from Mr. Coffey that it's a very small, limited group of experts who give cost of capital evidence in both the United States and Canada. Is that correct?
MR. COYNE:
A. Yes.
GREENE, KC:
Q. Okay.
MR. COYNE:

A. It's broader in the US than it is in Canada, in my experience.
GREENE, KC:
Q. And in your experience, do we all -
MR. COYNE:
A. But – I'm sorry. Do you mean in terms of the overall number of experts providing -
GREENE, KC:
Q. Yes.
MR. COYNE:
A. Okay. It's – in Canada, there are a number of experts that also provide, typically provide testimonies on behalf of intervenors, industrial groups, consumer groups and things of that nature. In our recent Alberta proceeding, I believe there were at least six, seven, or if not eight testifying experts in that proceeding on cost of capital. So, the number is broader if – those questions had to do with our competitors, those that are doing the type of work that we're doing, and I think the question pertained to those that are doing work for utilities and regulated utilities.
GREENE, KC:

Q. In your experience then, is the group of experts that we see at regulatory proceedings in Canada a small group or a large group?
MR. COYNE:
A. Well, I would say it's a relatively small group. Again, it's less than ten. But I think that number is probably not that much larger in the US. It's less than ten there as well, in our experience.
GREENE, KC:
Q. So, it's a fairly narrow group that provide this type of expertise in regulatory proceedings?
MR. COYNE:
A. I'd say that's fair, yes.
GREENE, KC:
Q. And in your experience, is it the typical practice that an expert will appear regularly for one interest group, whether it is the utility or an intervenor, such as a group of industrial customers or a group representing residential customers?
MR. COYNE:
A. I'd say that's fairly typical.

GREENE, KC:
Q. And would you also agree that it is very typical to see that the expert appearing on behalf of the utility usually provides the recommendations for the highest ROE to be awarded for the utility?
MR. COYNE:
A. As compared to an intervenor expert?
GREENE, KC:
Q. As opposed to the expert called on behalf of the residential user, such as the consumer advocate here.
MR. COYNE:
A. Oh, I think that's a fair characterization, yes. I think as exemplified by the recommendation of Dr. Booth in this proceeding and -
GREENE, KC:
Q. Which we have seen -
MR. COYNE:
A. - us in this proceeding.
GREENE, KC:
Q. Which we have seen in previous proceedings before the Board, and we'll talk a little bit about the proceedings in Alberta and BC,

but it is typical for the utility expert to provide the recommendation of the highest ROE and the consumer advocate expert to provide the recommendation for the lowest ROE for the utility?
MR. COYNE:
A. Well, when you have two experts, as you have here, that's almost always the case. If you have multiple experts, then you tend to have a range. Even amongst both utility experts and the intervenor experts, there tends to be much more overlap when you have multiple experts, as we did for example in Alberta. And in other jurisdictions, it's also the case that the Board hires its own expert and oftentimes that provides a third perspective.
GREENE, KC:
Q. Mr. Simmons talked to you about the degree to which providing opinions on cost of capital, the appropriate fair return, is an art or a science, and I tend to characterize it as exercising judgment versus objective facts and whether the amount of discretion that's involved. In your experience, is the

opinions provided by the expert influenced in any way by the clients that they typically represent?

MR. COYNE:

A. Well, it wouldn't be fair for me to characterize how others form their opinions based on their clients, but I can tell you how we work.

GREENE, KC:

Q. Okay.

MR. COYNE:

A. And that is that we have to be transparent with our analysis and our testimony, and we're also obligated to uphold obligations as being an impartial and expert witness, and that's why we lay out our analysis and our testimony the way that we do, so that it's transparent. All the data sources that we use are disclosed. Our work papers are provided. Our Excel working spreadsheets are provided. So, there is – I like to think that we're very transparent in reaching our recommendations and that we would reach the same recommendation regardless of who our client is. We don't –

our clients don't tell us at the outset, "this is the ROE we'd like to get from this proceeding". We run our models and provide our analysis and we say, "this is the appropriate ROE". So, we have to maintain our own integrity of process in order to be able to do so.

GREENE, KC:

Q. And you just mentioned the models that you've run and the methodologies that you use and primarily here you've used a CAPM model, the Discounted Cash Flow model and the Risk Premium Analysis model are the three that you have based your recommendations on for this proceeding, and I believe you indicated that these models are fairly standard models used by all of the experts. Is that correct?

MR. COYNE:

A. Standard models, but not used by all the experts. Other, Dr. Booth, for example, does not rely on a Risk Premium Analysis, as we do.

GREENE, KC:

Q. No. So, the choice of which models is a

matter of judgment of the individual expert. Is that correct?

MR. COYNE:

A. To some extent. I think virtually all experts rely to some extent on both a DCF and a capital asset – a CAPM approach. I think it is more discretionary, in my experience, to use the Risk Premium and the Expected Earnings. I would call these the second cousins to the DCF and the CAPM approach that are standard for most experts.

GREENE, KC:

Q. And in Canada, it is primarily the CAPM and some form of a discounted cash flow method that is primarily used. Is that correct?

MR. COYNE:

A. I'd say that's generally true. If you look to the BCUC decision that we recently testified, that Commission placed equal rate – equal weight on the CAPM, DCF and Risk Premium models that we provided to that commission, based on our recommendation, and they accepted equal weight on each of them.

GREENE, KC:

Q. But that isn't always the case. So, the

choice and the weighting to be given is also within the discretion of the expert and the regulator in making the decision by the regulator. Is that correct? For example, in Alberta, they did not accept the Risk Premium method.

MR. COYNE:

A. As I recall, they placed primary weight on the DCF and the CAPM models. I don't recall the weight on the Risk Premium. Do you, John?

GREENE, KC:

Q. We will come to the actual decision -

MR. TROGONOSKI:

A. Yeah, I -

GREENE, KC:

Q. - which you'll see they specifically rejected the Risk Premium model for consideration in their decision. So, again, when you look at the models, there's discretion as to which ones are used, accepting that the CAPM is primarily still the main one used in Canada. Is that correct?

MR. COYNE:

A. No. I'd say almost every jurisdiction in Canada now relies on the CAPM and the DCF in modern times.
GREENE, KC:
Q. Okay.
MR. COYNE:
A. I think in Canada, the CAPM was prevalent up until ten years ago, but it has evolved to the point where most Canadian jurisdictions now rely at least on the CAPM and DCF and with consideration of the other models as we just discussed.
GREENE, KC:
Q. And within the DCF model, there's also a discretion as to whether the constant growth method of the multistage method is accepted in Canada. Is that correct?
MR. COYNE:
A. That's right, and that's why we – we present both results recognizing that distinction, the multistage and the constant growth, and our recommendation here is based on only the multistage version of the DCF model. It's the more conservative approach. It also produces lower numbers.

GREENE, KC:
Q. And Dr. Booth, in his evidence, primarily relies on the CAPM method. Is that correct, using the DCF to test or verify the results of his CAPM?
MR. COYNE:
A. That's how he characterizes his analysis, yes.
GREENE, KC:
Q. If we go to your report, please, the original report, page 34 of the report.
MR. COYNE:
A. Mr. Trogonoski – on that issue, Ms. Greene, it might be worth noting that in response to the Consumer Advocate 196, we were asked this question about the prevalence of the models. I think we have useful charts there that show the prevalence in Canada and the prevalence in the US of the DCF, the CAPM, comparable earnings and other models.
GREENE, KC:
Q. Okay.
MR. COYNE:
A. And it compares them on a side-by-side basis in each country.

GREENE, KC:
Q. So, would you like to go -
MR. COYNE:
A. Yeah, it might be useful.
GREENE, KC:
Q. We can bring it up. Yes, yeah.
MR. COYNE:
A. I think it's a good question you asked. Consumer Advocate NP-196, if we could.
GREENE, KC:
Q. So, would you like to go down through the chart, scroll down?
MR. COYNE:
A. Please, yeah. So, this goes back to 2016. I was asked to give a presentation at CAMPUT on this issue and in that presentation, at that point in time, we researched which models were being used by regulators in both countries, and you can see the first chart shows the predominance of the DCF, followed by the CAPM, the comparable earnings or expected earnings and other, which is primarily the Risk Premium model in the US. And then if you go to the chart below, you can see that it was the prevalence of the

CAPM, followed by the DCF, the Risk Premium, expected earnings models in '16. And I think since then, we've seen, I would say, the bar on the DCF side has probably come up in Canada, based on our experience. So, I would say they're approximately equivalent at this point in time.
(10:15 a.m.)
GREENE, KC:
Q. And when you refer to the DCF model, are you making any distinction between the constant growth method and the multistage method?
MR. COYNE:
A. No. That would be either or both.
GREENE, KC:
Q. Okay. So, both would be in there. And have you done any analysis to show the difference in use between the two types of the DCF model?
MR. COYNE:
A. Have I surveyed each regulator on that?
GREENE, KC:
Q. I just wondered if you made the distinction for DCF for constant growth and DC – and the multistage model. Would we see more use in

Canada of the multistage, where it is accepted, versus the constant growth?

MR. COYNE:

A. Yes, more use of the – more acceptance of the multistage, and for that reason, we have relied exclusively on the multistage in our recommendation.

GREENE, KC:

Q. Thank you. No, that was helpful. If we could go to your report, page 34, lines 3 to 4?

MR. COYNE:

A. Page 34 did you say?

GREENE, KC:

Q. Yes, page 34 in your original report, lines – actually line 4, begin with line 4. And here you recognize that in doing the analysis informed judgment is used to assess the reasonable of the results and to determine the appropriate weighting. So, talk about a little more about the discretion that's used in the various models that are selected and into the inputs that are used into the various models and how what inputs you have used and whether

they've been accepted by other regulators. So there, as we've just discussed, you do acknowledge – you call it informed judgment and I may refer to it as discretion, but I mean the same thing. So, the degree to which informed judgment is used, as opposed to objective facts, even when you determine -- when you said you looked at, for example, sources for your beta from Value Line and Bloomberg, even the decision to do that is a question of informed judgment, isn't it? That not everybody would agree with, not the other experts and not the regulators that have looked at it.

MR. COYNE:

A. Okay. I'm going to try to answer your question, but I'm not sure that I understand exactly the question. So maybe could you just repeat it for me?

GREENE, KC:

Q. I guess the only – we can have a little bit of discussion about it, about how objective – because when you talk about the models and we use the formulas of the market risk premium multiplied by the beta, it makes it

sound so objective and so factual, but in reality, there's a lot of informed judgment or discretion used, either by the expert, and we'll see by the regulators because we have different decisions in Canada on the models, on the inputs, on the outcomes. So, the degree to which you would use your judgment in the selection of the inputs, how would you qualify the degree? Minor, balanced, significant judgment is used?

MR. COYNE:

A. I would say – well, in each of the models, as we have been discussing, we try to use a third-party source that's providing the data so that it's not our opinion as to what beta is or our opinion as to what the risk-free rate is. You won't hear that in our testimony and you won't see that in our analysis. There's some judgment involved in terms of using -- which forms of these models we use and the judgment there that we're using is one that reflects our discussions about how we hear Canadian regulators responding to this data. There are some issues that are controversial in

Canada that are not controversial before US regulators, and we respect that, and our evidence has evolved in Canada as a result of that, to reflect what I would characterize as more conservative interpretations of the models and their inputs, but we're still taking them from objective market sources. The two – probably the two distinctions where that shows up to the greatest degree is – and I'm sorry if this is not a simple yes-no answer to your question or balanced, but it's more important, I think, than I can do it justice with a simple answer to that.

But take the DCF model, for example. I would say there is no reasonable analyst that would recommend a form of the DCF model other than the multistage, and as we've shown in our – the difference between the multistage and the DCF is in the DCF applicant, the constant growth, the typical assumption is to use analyst growth rates and you assume that those last forever, right. The multistage assumes that those analyst growth rates only last for five years and then from there, you taper down typically to a GDP growth rate. As we've shown in our evidence, the companies in the proxy group have growth at a substantially faster rate than GDP over 20 years of history. Their earnings routinely outpace GDP. So, by taking future expectations of earnings growth and tapering them down to GDP, we're taking a conservative and low estimate of what those future earnings growth – the future earnings growth would be for these companies. So, that's a very conservative interpretation of that model. So, we're using judgment, but that judgment is leaning towards a more conservative result.

In the case of the CAPM model, there is a lot of debate concerning – and this just isn't in Canada, also in the US, concerning what the appropriate market equity risk premium is. So, we've taken the long-term history in both Canada and the US going back to 1926, and even though interest rates were higher then, we're treating that as the forward-looking market equity risk premium,

even though the forward-looking market equity risk premium is higher, as we show in our report.

So, we're taking the lower input on the market equity risk premium and the lower expected earnings growth rate in the DCF, both which move those results down, but we show both results so that you can see that impact. So, these are coming from third-party objective sources of market inputs and we believe that it's a strong basis for presenting this recommendation to the board, such as this one.

GREENE, KC:
Q. My only point is that in your selection of what to use, it has been different than, for example, what Dr. Booth has used in his with respect to how he has determined the growth rate to be used in the DCF model, and also how he has done the market risk premium, even when he looks at historic data versus how you have determined the historic data. So, there is judgment, and I can go back – I can take you to the BCUC decision too where you will see the choice of the inputs is a

matter of judgment by the expert providing the opinion and there is not unanimity or else we wouldn't have all these expert opinions with different ranges in them, different outcomes. Is that correct?

MR. COYNE:
A. There is not unanimity, and I think the biggest difference between the approach we take and Dr. Booth takes, for example, is that virtually every input or almost every input to Dr. Booth's analysis, both on the DCF side and on the CAPM side, is based around a judgment that Dr. Booth is making. Now, he's not – he's providing his opinion around what beta is, for example, by looking at a lot of history over beta as opposed to taking a Bloomberg or Value Line estimate as we have. So, I think that yes, there are differences of opinions between experts, but I like to think that when you're taking it from a third-party source that you can at least provide a board or commission with the source of that data, where it came from and the basis for it, which I believe doesn't have to rely on an expert's opinion.

GREENE, KC:
Q. We go through some of your, the inputs. The first one I wanted to look at is your choice of a North American proxy group.

MR. COYNE:
A. Um-hm.

GREENE, KC:
Q. And your recommendation is that the North American proxy group is the most relevant to support the recommendation. Is that correct?

MR. COYNE:
A. That's right, even though we provide results for both the Canadian and US proxy group as well.

GREENE, KC:
Q. And as we've heard some discussion already, the use of American data has been one of the issues that has been controversial over the years in Canada and I believe you indicated that there is a more recent trend to accept the use of US data. Is that correct?

MR. COYNE:
A. That's right.

GREENE, KC:

Q. If we could go to PUB-NP-115 please?
MR. COYNE:
A. Could you repeat that? Which one?
GREENE, KC:
Q. PUB-NP-115. You have referred to it already in your testimony. So, this was the question that was asked because the Board, the last time that we actually went to a hearing on cost of capital in 2016, decided that there should be a downward adjustment to reflect the difference between the US and Canadian experience, and I wanted to give you the opportunity here to provide a further explanation as to why the use of the US proxy group and US data doesn't need adjustment. You've already mentioned it briefly already, but here you – had there been any change since the previous decision, and I guess, here you refer to a recent decision from British Columbia. Is that correct?
MR. COYNE:
A. Yes.
GREENE, KC:
Q. And why was that significant for you?

MR. COYNE:
A. Well, it was an opportunity to re-examine this issue in a substantial way and not just BC, but beginning I'd say with Ontario back in 2009, there's been an ongoing exam – and prior to that, the NEB as well – an ongoing examination of the use of US proxy companies for these determinations. And increasingly, I think virtually every regulator in Canada at this point in time accepts the use of US proxy companies for this basis. So, that's no longer a question as to whether or not it's reasonable to use US companies for this analysis, I do not think, based on our experience at least. The question remains for some as to whether or not some adjustment is necessary, as in your question, and as we have looked at this issue, and you know, we'd look at the integration of capital markets. We'd look at the integration of the industries. New capital is raised on both sides of the border and the substantial investments that are made both by US companies in Canadian jurisdictions, but more so Canadian

companies in US jurisdictions, as providing an integrated industry, operating in an integrated – increasingly integrated North American capital market. So, for that reason, we do not think it's necessary to make an adjustment on this basis.

It's interesting that this issue was argued before the NEB about 20 years ago and at that point in time, it was argued that there should be a premium for Canadian companies over US companies, the opposite argument basically, and that argument was rejected then for this reason and I think it's still appropriate to consider the US proxy group integrated with Canadian companies, as we've done here, and you can actually show the data both ways, for Canadian proxy group with Canadian data and a US proxy group with US data, as well as the North American version, so the Board has the opportunity to see what impacts it would have.
GREENE, KC:
Q. So, the question, from the time we were here in 2016, the change, you did – relates to –

and that's why you referred to it, a more recent decision from British Columbia, and we'll see one from Alberta as well, with respect to the use of US data. I just wanted to confirm with you that the decisions you refer to from Ontario and the National Energy Board were before 2016 and were also used by you at that time before the Board to justify the use of – of the acceptance of the fact there should be no adjustment to US data. Is that correct?
MR. COYNE:
A. That's right, yeah. I see it has been – it's an evolution of acceptance that's occurred in Canada.
GREENE, KC:
Q. I wonder if we could go now to the BC decision. It was circulated last week to the parties. I believe the parties indicated they did not need a copy. We have copies available and I would like to enter it as an information item.
(10:30 a.m.)
MS. GLYNN:
Q. No. 23.

GREENE, KC:
Q. No. 23. Copies were provided electronically last week and the parties were asked if they wanted copies and indicated they did not. So, just a brief discussion of this. If we could go to page 16 of this decision.
MR. COYNE:
A. 1-6?
GREENE, KC:
Q. No, 16, 1-6.
MR. COYNE:
A. 1-6.
GREENE, KC:
Q. At the very bottom of the page, okay. Now there are no line items here, but if you look at the last paragraph, we do see this – the second sentence in that last paragraph, the Board – and this is the Board. The we is the Board in British Columbia. They did agree that there was amble basis to include US data. So, there they did agree in that they did agree to look at the results from the US proxy group, which is what you have said. Now let's go to the next page, page 17, and I'd like to read the first full

sentence in the next paragraph, which is "as for the weighting of the ROE results among the North American proxy group, as between the Canadian utilities and the US utilities, we find that to be largely a matter of judgment that is within our discretion".
MR. COYNE:
A. Yes.
GREENE, KC:
Q. Now again, while there's a recognition that the data may be helpful, there certainly was also an indication that there is a matter of judgment that the regulator will take into account how to use the data. Is that correct?
MR. COYNE:
A. That's right, and the Board accepted our screening criteria that we were using and which resulted in fewer Canadian companies as a result of that. And so, we ended up recommending a North American proxy group that removed non-comparable – what they called non-qualifying Canadian companies because they weren't sufficiently either electric or gas enough to be representative

of the gas or electric utility here in question.
GREENE, KC:
Q. And one of the reasons for looking at the proxy group, including US companies, if we go back to the previous page, is because of the limited number of similar comparators in Canada, is that correct?
MR. COYNE:
A. That's right, yeah.
GREENE, KC:
Q. Okay. Can we go to rebuttal evidence, please, page 6.
MR. TROGONOSKI:
A. Page?
GREENE, KC:
Q. 6 of your rebuttal.
A. 6? Oh, of our rebuttal?
GREENE, KC:
Q. And here if we could go to line 13. So, above that you do refer to the BC decision. Actually, we should scroll up to the top of the paragraph because it deals with how US data should be considered by the Board. So,

there you do say that British Columba--in the British Columbia decision we just looked at, they didn't make an adjustment for US data, line 9 to 13. So, we just saw that the regulator also said that while you can look at US data, there is still a fair amount of discretion or judgement that must be used in how you assess the results.
MR. COYNE:
A. Yes, and the judgement they applied is that the North American Proxy Group was most appropriate, which only included a couple of Canadian companies because they were deemed to be most comparable. So, it was predominantly a US proxy group, but with appropriate Canadian companies that were added, and I think there were two that satisfied the Board's criteria in that regard.
GREENE, KC:
Q. Yes, but they went on to say that in determining the appropriate ROE there was still judgment to be exercised -
MR. COYNE:

A. Yes, there's judgement applied by the Board.
GREENE, KC:
Q. - about how to use the US data. So, if we now to go the second –
MR. COYNE:
A. How to--which companies to include in that case is what they were talking about.
GREENE, KC:
Q. As to the weighting of the--just go back to the US decision. I mean, I'm sorry, the BC decision we had up there. I guess it's an interpretation of the Board's words. "As for the weighting of the ROE results that's among the North American Proxy Group, as between Canadian/US utilities we find that to be largely a matter of judgement that is within our discretion." So, when I read that I understood that the Board, yes, they would--how I interpreted it, and perhaps we should see if you interpreted it differently, is that even though they looked at American companies to see what the information was because it was useful data, they go on to say how they weighted the

results from that group, it was to be a matter of judgement that was still within their discretion.
MR. COYNE:
A. Well, I think that sentence stands on its own, and I was going on our experience before the Board and the entire discussion where they talked--they're focused on which companies to include as arriving at their decision there is how I see the big picture, but I see what you're saying about their sentence.
GREENE, KC:
Q. So, if we go back to your rebuttal evidence, so you referred to the BC decision and you also then at line 13 go on to say that similarly the Alberta Utilities Commission also relied on a North American Proxy Group without making an adjustment for US data in its October '23 decision on generic cost of capital. So, you're relying on both BC and Alberta decisions to support your position there should be no adjustment or no discretion used with exercise, with how US

data is used because it's so similar to Canada, that the North American Proxy Group is the most relevant. So, now -
MR. COYNE:
A. That's not my position.
GREENE, KC:
Q. Oh, sorry.
MR. COYNE:
A. That's not my position. You said I've relied on these decisions--well, if you could repeat your question, but I think the way you characterized it is not our position. Perhaps you could just repeat the question.
GREENE, KC:
Q. When I read your evidence and the answer to the RFI, and now your rebuttal evidence, I took--what I took from it was that you were using the two recent decisions from Alberta and BC to support your opinion that the North American Proxy Group is the most relevant and reliable one for the Board to consider in setting the ROE for Newfoundland Power, and that in doing so, they didn't

need to make adjustment for US data, that it was no need to do that. That's how I took what--and you use those two decisions to support your opinion which you have expressed since you have been the Cost of Capital Expert for Newfoundland Power.
MR. COYNE:
A. Well, our opinion is based on much more than that. We provide substantial evidence on the integration of North American markets, integration of the industries. So, we cite those as examples of how other regulators have approached this issue, but that's not the sum basis of our evidence that that's the right thing to do.
GREENE, KC:
Q. And I didn't mean to imply that. That you are using that as additional support for your position, you have expressed and to reflect the fact that the situation in Canada is evolving, that more regulators are going towards the use of American data.
MR. COYNE:
A. Yes, I think that's a fair characterization.

GREENE, KC:
Q. Sorry. That's what I had meant from before. Okay. So, if we can go now to the Alberta decision, which also was circulated last week, and I'd like this filed as an Information Item.
MS. GLYNN:
Q. The Alberta decision will be Information number 24.
GREENE, KC:
Q. So, I'd like to go to page 22, and if we could go up to, yes, the paragraph 103. There reading from that, "While the Commission finds that the US companies have higher business risks than the Alberta utilities for the purpose of establishing the comparative group, the Commission accepts the utility's evidence that it is appropriate to include US holding companies," and they go on to give the reasons for doing so, which I won't read, but then they go on in paragraph 104 and say, "After considering the evidence presented in this proceeding, the Commission

acknowledges that the utilities in the comparator group are not identical to the Alberta utilities, but concludes they are sufficiently comparable for use in the various financial models. And then we go on down. They go on to say that, "The Alberta utilities at the low end of the range of risk presented in comparator groups, and accordingly the Commission retains the view as expressed in the 2018 generic cost of capital decision, that a significant amount of judgement must be applied by the Commission when interpreting data from representative utilities to establish the ROE required by investors in the Alberta utilities." So, again, there was--do you agree, Mr. Coyne, that there was an acknowledgement by the regulator there that again a significant amount of judgement had to be applied in interpreting the data even though they had considered American companies, or the North American Proxy Group, for the purposes of analysis?
MR. COYNE:

A. Yes, I think that statement stands for itself. If you look at the context of this being involved in that proceeding, they did it in two phases, if it would be helpful for the Board to understand where they were coming from. They had a technical conference where experts participated representing utilities and intervener groups to decide which companies should be included in a proxy group for this analysis, and we participated in that process. I don't know if you remember how many companies were included in the proxy group, but it was a broad number of US electric and gas utilities, and I think the five or six Canadian companies that could be included.
MR. TROGONOSKI:
A. Yes.
MR. COYNE:
A. But it was –
MR. TROGONOSKI:
A. I think there were 33 companies in total.
MR. COYNE:
A. In total.

MR. TROGONOSKI:
A. Five were Canadian, and 28 were US.
MR. COYNE:
A. And then they allowed each expert to provide evidence in the second phase of this using their discretion in terms of that proxy group and the models they would use to provide expert evidence around ROE and the continuation of the formula. And when they looked at the evidence submitted by the experts, they were of a view that the Alberta utilities--for one reason, the Alberta utilities don't have the merchant flexion, so they don't--they're not suppliers, they're a distributor, they're T&D companies only. They don't have a supply responsibility as does Newfoundland Power. So, they decided that for various reasons their view was that Alberta utilities were at the low end of the risk spectrum. So, when they considered the DCF model, for example, it was their view that the low to the mean estimates of earnings growth would be appropriate representing the

lower risk of Alberta utilities as they saw it. So, those are the kind of judgements they applied having reached the conclusion that Alberta's utilities, while that proxy group was appropriate, that they were at the lower end of the risk spectrum. That's the context that I see within this overall discussion and based on also the experience from the Board.

GREENE, KC:

Q. Yes. So, the reason to refer to these decisions is the fact that even though American data was considered in the two recent decisions, there was also acknowledgement that there's still a significant amount of judgement that has to be applied to how the data is used. And, in fact, if we go through them, we may go through a couple of how Alberta considered your recommendations with respect to the market risk premium use of adjusted betas to see that they also exercised their judgement and how that was going to be applied to the proxy, proxy group that included American

companies.

MR. COYNE:

A. I'm sorry, was there a question?

(10:45 a.m.)

GREENE, KC:

Q. I'm just saying, you had said they did--you went on to explain how risk was taken into account, and I made the comment that we will also see how they took into account the American results in looking at the use of betas and market risk premiums, and how they should consider American data for that as well. So, that was my only comment. So, the other--if we go back to your original report, page 3, Figure 1 -

MR. COYNE:

A. I'm sorry, the direct report?

GREENE, KC:

Q. Yes.

MR. COYNE:

A. Okay, and which page?

GREENE, KC:

Q. Page 3.

MR. COYNE:

A. Page 3?

GREENE, KC:

Q. Page 3, yes. I just want to explore with you a little bit how you exercised your judgement in coming to your recommendation. Here we see the methods used, and this is not where you ended up with your recommendation that you presented the results to show the Board what the results would have been if the constant growth DCF method was used, and multi-staged DCF, the average CAPM, the risk premium applied to each of your proxy groups, is that correct?

MR. COYNE:

A. That's right.

GREENE, KC:

Q. Now, if we go to the next figure, and this is illustrating the basis of your recommendation, is that correct?

MR. COYNE:

A. Yes.

GREENE, KC:

Q. In formulating your recommendation, even though you showed us the results of your

constant growth method which you had last in your previous opinions provided to the Board, why did you remove the constant growth method here?

MR. COYNE:

A. Because we know that in our experiences we discussed a few moments ago, it is not universally accepted by Canadian regulators that the constant growth assumptions the DCF model are reasonable, and we find that to be less controversial in the US, but in recognition of that issue in Canada, we have used only the multi-staged DCF in order to present what we believe was both eliminating that controversy, and presenting what we believe is a reasonable interpretation of the DCF model.

GREENE, KC:

Q. And that is one of the--would you agree that that is one of the ways in which you have exercised your judgement in formulating your recommendation?

MR. COYNE:

A. Yes, we've taken the more conservatory route to using the DCF model, and that's consistent with the two decisions that we just looked at in BC and Alberta.

GREENE, KC:

Q. And the risk premium method that's there, I think you mentioned earlier that that may not be universally accepted as a method to use in determining the appropriate ROE, is that correct?

MR. COYNE:

A. Yes, that's right. With the risk--with the CAPM and the DCF model we can use a combination of Canadian companies and US companies to form a North American Proxy Group, and you'll see that we don't have a risk premium result for Canadian utilities there because up until now we haven't had the same database of decisions in Canada that would allow us to estimate a Canadian risk premium model. The way that model works is you regress the relationship between allowed returns by regulators and bond yields in order to show what that relationship has been historically, and if

regulators were consistent in making those determinations, how they would determine ROE based on current or projected bond yields. So, it's an inherently US approach as a result of that, and some commissions have been less comfortable with the risk premium approach as a result of that. That's not true with BC. The BC Commission placed equal weight on the risk premium model, and I would say that we have been compiling a database now of Canadian utility decisions where we're now able to compute a risk premium model. So, that's about to change for us. We're finally in a position where we can do that using Canadian decisions and Canadian bond yields.

GREENE, KC:

Q. The risk premium model wasn't accepted by this Board back in 2016 as a method to use in determining the ROE, was it?

MR. COYNE:

A. No, I don't believe it was.

GREENE, KC:

Q. And was it accepted by the Alberta Board in

its recent October 2023 decision?

MR. COYNE:

A. No, I don't believe it was.

GREENE, KC:

Q. No. It was specifically rejected, wasn't it? We can go to the decision if you would like to see that.

MR. COYNE:

A. Do you have any different –

MR. TROGONOSKI:

Q. No, I don't.

MR. COYNE:

Q. I think we're in agreement.

GREENE, KC:

Q. If we eliminate the risk premium model from your Figure 2 summary, the overall average declines a bit doesn't it, because the risk premium is the highest one there, the results for US and North American?

MR. COYNE:

A. Right. We could compute that number if you like.

GREENE, KC:

Q. Yes, that would be helpful. Should we mark

that as--are you going to do it now?

MR. COYNE:

A. Sure.

GREENE, KC:

Q. Okay.

MR. COYNE:

A. It's just two numbers. Even I can handle that on the stand. I trust myself doing that. I have somebody who will check me here.

MR. TROGONOSKI:

A. I think it would be 9.64.

MR. COYNE:

A. So, you did it in your head. I'm impressed. This is youth for you. I'll just my trusty calculator, but I trust Mr. Trogonoski. I confirm that result.

GREENE, KC:

Q. The 9.6?

MR. COYNE:

A. 9.64 if you just used the two models.

GREENE, KC:

Q. So, if we--so, if you take out that it would be for the Canadian utility group, the

average would be what?
MR. COYNE:
A. Oh, for the Canadian utility group?
GREENE, KC:
Q. Let's do that one first.
MR. COYNE:
A. For the North American Proxy Group it would be 9.64 if we just used those two models. We only had the two models for the Canadian group, and that's 9.87 as you can see there, yes.
GREENE, KC:
Q. Okay. So, let's just confirm again I'm sorry. It's--for the US Electric Proxy Group it would be –
MR. TROGONOSKI:
A. I think it would be 9.77.
MR. COYNE:
A. There you go.
GREENE, KC:
Q. And for the North American Electric Proxy Group?
MR. TROGONOSKI:
A. That would be 9.64.

MR. COYNE:
Q. Are you doing that in your head, or did you already figure that out, but he's right.
GREENE, KC:
Q. If we look at the historical CAPM method, you have adjusted how you have done that from the last time you were here, is that correct?
MR. COYNE:
A. That's right.
GREENE, KC:
Q. Can you just explain briefly the adjustment that you did?
MR. COYNE:
A. Oh, the adjustment? Previously, as I recall, we took an average of the forward looking and the historical market equity risk premium, and in this case we've used only the historical, and we've done that for two reasons. One is that the earnings growth projections for the broad market are fairly robust. Coming out of COVID they're pretty strong expectations for earnings growth for the S&P 500 companies, or the TSX

companies, and we see an increasing gap between the projections of earnings growth and what they have earned historically. So, when we check it against the historic data, the market equity return is much lower, and we know that that's also been a source of controversy before Canadian regulators, even though as--it's a model that has been adopted by FERC in the US after substantial litigation around the issue of whether or not forward or historic looking market equity risk premiums were more appropriate. FERC accepts the forward looking only without any reliance on history, but again, to our more conservative approach here, we've used only the historic market equity risk premium to take that controversy off the table, and it gives you a lower and more conservative result as a result of that input.
GREENE, KC:
Q. So, again, it is a change from your previous expert opinion when you were here in 2016, and that's another example of how you have

exercised your judgement in coming forward with the recommendation for the ROE?
MR. COYNE:
A. That's right, and consistent with what we said earlier about reading orders and understanding what commissions have found to be reliable and credible for these purposes.
GREENE, KC:
Q. Another input into the CAPM method is of the use of a beta. Do you want just to give a high level description of what beta is, very general? I'm not going into any detail with you. It's like Mr. Simmons, I'm not quite sure I understand them either. I understand how people have treated them, but -
MR. COYNE:
A. Well, I'm not doing my job if I can't explain it in terms for those that don't do this every day. The Capital Asset Pricing Model, or the CAPM, has three primary inputs, and it's based on a fairly basic premise, that an investor would require a return that's equal to the Risk Free Rate, and the Risk Free Rate is typically the

government bond yield, 10 or 30 years. For most utility matters we use 30 years because that is the expected life of utility assets, it's typically very long term. So, it's equal to the Risk Free Rate, plus some adjustment for risk associated with a utility investment. And the way that we get at that is we look at the overall return on the market, and as we just discussed, that's the market equity risk premium. So what does market overall require as a premium over the risk free bond yield. And as we were just discussing, we take that as the history of all market equity risk premiums in the Canadian/US markets over time as being reflective of what we think investors will expect in the future. And then we multiply that by beta. And what beta does is, it says you're not trying to return--you're not trying to calculate the expected return for the overall market, which is the risk free rate plus the market equity risk premium, we want a utility. And in order to get at the utility, beta is the multiplier.

And what beta does is it determines the relationship between the stock prices for utilities and the stock prices for the overall market, and if those stock prices are less volatile in relationship to the overall market, that's deemed as being a good thing, and therefore beta will be less than one. So, the typical beta adjustment is the overall market return times the beta adjusted downward for utility because they're a safer and a little bit less volatile than the overall market. And now it becomes an issue of how do you estimate that beta, and the way that we estimate beta is we take two sources. One is Value Line, because they publish investor reports that are widely used, and they use five years of weekly betas in relationship to the New York Stock Exchange, and then they calculate--or the TSX in Canada, and that's how they calculate their beta. So, it's utility stocks moving in relationship to the TSX or the New York Stock Exchange, five years of data, weekly observations. We use the same-

-we derive the same beta calculation from Bloomberg, but Bloomberg uses the S&P 500 as the basis for the TSX. So, it's a slightly different market measure, but they move so closely together that you get very comparable results, but in both cases it's five years of data used to determine what that relationship is between utility stocks and the overall market, and those are the three inputs to the CAPM model.

GREENE, KC:
Q. And while people agree with the need to reflect the risk of a utility versus the overall market risk, which is the use of the beta, what the actual beta is and how it's calculated is one of the most controversial issues in looking at the CAPM result, isn't it?

MR. COYNE:
A. Only in Canada.

GREENE, KC:
Q. There's lots of things only in Canada, whether it's our orange pekoe tea; only in Canada.

MR. COYNE:
A. I didn't hear your comment. Could you repeat it?

GREENE, KC:
Q. It's a Newfoundland expression I think certainly. Orange pekoe tea, and I'm not even a tea drinker, but there used to be an ad that said, "Only in Canada," and that's what you reminded me of.

MR. COYNE:
A. Well, I enjoy orange pekoe tea. When I say only in Canada, let me tell you more about what I mean. This is an issue that is widely accepted in the investment community, investors that we work with. It's generally considered to be the use of an adjusted beta that's adjusted according to the "Blume Methodology", and the analysis behind that shows that beta can be raw, and that is what you estimate from the market data, and that over time betas that are adjusted towards the market mean one, will do a better job of predicting how the stocks are actually going to behave in the market, and then there's

some other statistical reasons to do that as well, and that's called the Blume Adjustment Methodology. And I know we have in an IR comparison, maybe John can find it here, of raw betas and adjusted betas to show you the difference that that makes, but before US regulators, in our experience, these adjusted betas were into the Blume Methodology are the standard, and it's typically not a controversial issue.

(11:00 a.m.)

GREENE, KC:

Q. But it is in Canada, isn't it, another difference here between the Canadian regulatory environment and the US regulatory environment? I can take you through decisions where--and we will actually go through a couple where it is not accepted in Canada to use adjusted betas.

MR. COYNE:

A. Well, again -

GREENE, KC:

Q. In the manner that you have recommended.

MR. COYNE:

A. Most recently in the BC decision, the BC-- the BC Commission relied on our use of these adjusted betas, and they were also endorsed by the Board's expert. So, that was not--I would say that that was not a controversial outcome from my perspectives in that proceeding, but it has been--it has been an issue in other Canadian proceedings as to whether or not they should be adjusted, and if so, by how much. What's happened is interesting because raw betas have come up substantially for utilities over the course of the last five years, and as a result of that, the difference between an unadjusted or an adjusted beta is much smaller than it used to be. So, to the extent the risk controversy there, it's less important than it used to be, and I think if we turn to page--that's just in our rebuttal testimony. This would be the Figure 5 on page 29 in our rebuttal testimony, is probably the best way to look at that. So, knowing that this is an issue of concern perhaps for this Board as it has been in the past, we compared raw

and Blume adjusted betas, and it's the Blume adjusted betas that we're using to show you what those differences are, and if you look at the North American Proxy Group that we're using, you can see that for the most recent data that we're relying on through April of '24, that different is .82 versus .88, and that's narrowed some from where we it was when we prepared our direct testimony, which is .79 versus .86. So, that's with no adjustment whatsoever. And using the Blume adjustment it takes it up by 7 basis points back in August, or 6 basis points now. And the reason for that is that the betas for utility companies have moved much closer to the market, and there are various interpretations of that, but one interpretation is that the market views utilities as being riskier than they have in the past. If you go back to January 2020, you can see that the betas were lower on both sides, both raw and adjusted, more in line with the view that Dr. Booth has taken on what betas are, but in our view those

don't reflect the current market data that shows that betas have moved up substantially since then.

GREENE, KC:

Q. We're past our break time.

CHAIR:

Q. Okay. We'll take a break now. Thank you.

(BREAK – 11:04 a.m.)

(RESUME - 11:51 a.m.)

CHAIR:

Q. So we're back to Ms. Greene.

GREENE, KC:

Q. Thank you, Mr. Chair. When we adjourned for the break, we were talking about betas and the role they play with respect to the CAPM method, and I just wanted to take you, it's the last question on the use of betas in the CAPM method to the decision from the Alberta Utilities Commission which is Information No. 24, page 28—I'm sorry, before the break I believe you mentioned that in British Columbia the commission did accept the use of Blume adjusted betas and I just wanted to also refer to the decision from Alberta and beginning at paragraph 129, and here in the decision by the commission they note that—I'm just reading from the first sentence in paragraph 129, "For example, the commission remains uncertain of the extent, if any, to which the Blume adjustment is warranted in determining betas for regulated utilities that face less risk than an average firm in the market. Indeed there are ample reasons to question on what basis the systematic risk faced by regulated utilities might ever be expected to approach, much less exceed those for the market as a whole, which is a central premise of the Blume adjustment." And the Blume adjustment is what you have used in your recommendations, is that correct, Mr. Coyne?

MR. COYNE:

A. That's right.

GREENE, KC:

Q. And then we go on down to paragraph 132 where they do conclude that utility stocks are appreciably less risky and volatile than equities in the broader market and they go on to look at the range of betas between .45 and .75 in that case. So again, just to

confirm that whether betas get adjusted and by how is one of the issues that remains a bit controversial or is controversial here in Canada, is that correct?

MR. COYNE:

A. Well it is, I think the AC decision stands for itself and maybe to your point if you look at the BC decision, they arrived at a conclusion that the Blume adjusted betas were reasonable, so maybe that is your point, that not every regulator sees this the same way. One thing to bear in mind, though, is that the betas have come up since then. This was based on market data that was over a year ago, so both raw and adjusted betas have all come up since that period of time as we discussed in our earlier questioning and the chart that we showed, I think it was in our rebuttal testimony, that shows you the difference between a raw and adjusted data, so both were available for the Board.

GREENE, KC:

Q. And we have evidence before the Board from both you and from Dr. Booth with respect to

recommended betas to use in this particular case, but again, as we've gone through some of the inputs into the various models, we do see that there is significant, in my view, discretion or judgment used by experts and by regulators in terms of the inputs to the various models that are used. One last question –

MR. COYNE:

A. I'm sorry, was there a question?

GREENE, KC:

Q. No, an observation. I wouldn't ask you to agree. One last question on area on your recommended return on equity. You have stated in your evidence as filed and also in your testimony that the capital market conditions have changed since you were here last and that also is a factor that needs to be taken into account, and I believe Dr. Booth also agrees with that point. Last time you were here, your recommended ROE for Newfoundland Power was 9.8 on a 45 percent equity in their capital structure. This time your recommendation is 9.85, so how do we take your difference in your

recommendation of only 5 basis points, if you accept that the ROE here of 8.5 should be a bit higher because the capital market conditions have changed, indicating the reason of requirement for a higher ROE, is the range in that vicinity of 5 basis points that the Board should consider?

MR. COYNE:

A. I think the appropriate range for the Board to consider should be that's based on the current market data, as presented in our evidence and if you look to, if you look to page 86, if we could go there in our direct testimony, Figure 43. Thank you. So the range from the North American proxy group is 942 to 10.26 and an average of 985. To me, that's the range that the Board should be considering and the basis for our recommendation is the average result from the three models. So I think that's the appropriate range based on current market data and as we've discussed, there have been changes both to our approach, as well as the market data utilized between 2016—was your point of reference 2021, '22?

GREENE, KC:
Q. Well since the capital market conditions have changed in your last recommendation which was the 2022 GRA.
MR. COYNE:
A. They have, yes, and we have a chart that shows those changes.
GREENE, KC:
Q. Yes, and I don't mean to go through it, I was trying to understand, you recommended 9.8 last time; this time you say the capital market conditions have changed, but you intuitively might have thought that your recommended ROE therefore would be higher than just 5 additional basis points.
MR. COYNE:
A. Yeah, there have been some offsetting factors and development of that recommendation.
GREENE, KC:
Q. Okay, so the other inputs have changed into how you have done the analysis for the various methods you've used.
MR. COYNE:
A. That's right.

(12:00 p.m.)
GREENE, KC:
Q. I wanted to move now to a different topic which is first if we could bring up PUB-NLH-003. And we'll come to a RFI that was also asked of Concentric with respect to the implications, if any, on their recommended ROE and capital structure for Newfoundland Power that arises from the impact on Newfoundland Hydro and on rates for customers arising from the flow-through of the Newfoundland return on equity that flows through to Hydro as a result of various contracts that are in place. So if we could go to the next page, page 2, we see there in the last paragraph that a change in Newfoundland Power's ROE of plus or minus .5 percent changes Hydro's payments under the Transmission Funding Agreement by 11 million per year on average and in addition there's other flow-throughs other than just the Transmission Funding Agreement that would be impacted, so the overall change for each half percent change is Newfoundland Power's ROE is another 13.6 million dollars which

would be added to Hydro's revenue requirements to be recovered from customers. So the question now, if we could go to PUB-NP-134 and I'm not sure, have you seen this elsewhere where a change in the return on equity for a utility would have that automatic flow-through to another utility and then onto customers, so the question was given this situation which may or may not be unique, how, from a regulatory perspective, should the Board take into account that their decision for the Newfoundland Power return on equity also will cost Newfoundland ratepayers a significant increase over the longer term? Is that a relevant consideration for the Board to take into account? And that was the RFI, refresh your memory, with your response.
MR. COYNE:
A. And, Ms. Greene, your question is is it a relevant consideration?
GREENE, KC:
Q. Yes, that the Board should take into account in their consideration of the appropriate fair return for Newfoundland Power.

MR. COYNE:
A. The impact it would have on Hydro's rates.
GREENE, KC:
Q. And then ultimately consumers in the province.
MR. COYNE:
A. And consumers. And your question is is that a consideration that the Board should take into account.
GREENE, KC:
Q. In setting the fair return for Newfoundland Power and your opinion has been provided on what that fair return should be.
MR. COYNE:
A. Well, you know, as discussed earlier I think the Board has two sets of responsibilities. One is to set a fair return in this proceeding for Newfoundland Power and in doing so, it's guided by the fair return standard and the North Western principles that form the fair return standard. But I think the Board also has a broader set of responsibilities when it comes to setting just and reasonable rates and the Board has, you know, without going through its

legislative requirements, I think the Board has to take a big picture view of the impacts of all of its actions on customers, consumers and the broader welfare of the province, so I'd recognize that it has two sets of responsibilities in that regard.

GREENE, KC:
Q. But with respect to the fair return standard, given that we have seen there is significant, I'd say significant, you may disagree, judgement or discretion into determining what is a fair return, you believe, I take from your answer you believe that that is a factor that in the broader context can be considered, the flow-through –

MR. COYNE:
A. Well I think the Board needs to understand the implication of its decisions on all consumers and how they are impacted. The Board has a difficult set of responsibilities in that regard and that's why I found solace in the fact that it does have these fair return standard requirements that it can use and then within those

standards, it has to exercise its informed judgment in determining what a fair ROE is. So I would agree with all of those things. We think that that fair ROE is 9.85 percent based on the analysis that we've conducted, but I recognize the Board has to take into account all of those considerations.

GREENE, KC:
Q. Moving to my last area of questions, you recommended in your evidence and it has been accepted by the parties in the Settlement Agreement that the automatic adjustment formula will continue to be suspended at this point in time, is that correct?

MR. COYNE:
A. Yes.

GREENE, KC:
Q. Based on your experience, if there is no automatic adjustment formula and here Newfoundland Power is asking for rates to be set based on two test years, what would your recommendation be with respect to years subsequent to 2026 in this particular case, from a fair return standard?

MR. COYNE:

A. Well we have, we have used, as practical, we have used forward looking market data in reach our recommendation, so I would think that the 9.85 percent that we recommended would be appropriate over a three-year rate period and I understand that that, that implies some risk that markets change, both up or down, between now and then, but I think that's a reasonable period of time over a company, that a company, such as Newfoundland Power, should be able to manage within that rate period.

GREENE, KC:
Q. And so if we continue and it would be up to the utility if it determined that it was impossible for it to make its fair return to make a new application to the Board for new rates based upon a new test year, is that how I take your answer?

MR. COYNE:
A. That's my understanding of the option it would have here, yes. Unless it committed to, you know, some other period that it would come back in for a rate review. And Mr. Trogonoski is reminding me that we've

answered that question in response to NP-130 where we recommended the return be continued in 2027, absent to change by the Board, so I think that's consistent with what I said.

GREENE, KC:
Q. The automatic adjustment formula has been suspended here for a number of years and in a previous Board order, the Board ordered Newfoundland Power, in their third year, to file a rate of return application, so based on what I understood your answer to be, you probably think that would not be necessary and would not be regulatory practice?

MR. COYNE:
A. In the third year.

GREENE, KC:
Q. 2027 if we could talk about specifics here.

MR. COYNE:
A. Yeah, so I'm sorry, just so I understand your question, so is your question whether or not the Board should require the company to come back and make a new rate application for 2027?

GREENE, KC:
Q. No. The practice here has been the Board

has asked them in the third—since the formula has been suspended to file an application in the third year indicating what the rate of return would be for the third year. I'm not sure if I need to go into any more details in that about it, but I took from your answer that if the Board did not order that this time, which of course is certainly up to the Board, the normal practice would be that then in the third year these principles that would set in this GRA would apply and it's up to the utility then to determine if they needed to file anything for the third year.

MR. COYNE:

A. My view is that's fair and that's consistent with the thought we gave to that approach, and I like, I think capital markets are more stable than they were back during the COVID period, and so, I think a three-year period of reliance on a ROE in today's markets is reasonable. So my view is that it should not be necessary to revisit that until year four, as I understand your question.

GREENE, KC:

Q. Yes, thank you very much. That concludes all my questions, Mr. Coyne, Mr. Trogonoski, thank you very much.

MR. COYNE:

A. You're welcome.

CHAIR:

Q. So it's up to us?

GREENE, KC:

Q. Yes.

VICE-CHAIR NEWMAN:

Q. No questions, thank you.

COMMISSIONER O'BRIEN:

Q. No questions.

CHAIR:

Q. I've got a couple of short ones. One of the ones I struggled with, now it's a pretty complex topic you got, so there's probably a lot of things I would struggle with, but I was, a direct question with regard to how does the stronger capital structure of Newfoundland Power influence your recommended return on equity?

MR. COYNE:

A. When we look at the overall analysis, we come to both a ROE recommendation and a

capital structure recommendation, and then we look at the underlying credit worthiness of the company and we look at ROEs and capital structures of the peer companies, both in the proxy group, as well as the Canadian operating companies, and our view on that is that the capital structure that's been in place for Newfoundland Power has served it well, it has maintained a strong credit rating during a variety of economic capital market conditions and I think that the Board, in my view, is probably somewhat forward looking when it established the equity ratio that it did for Newfoundland Power, recognizing some of the risk characteristics that are still associated with the utility and I see over time that, I think other Canadian regulators will probably be catching up to where this Board has been in terms of bridging some of the gap between where Canadian companies have typically operated and where the US companies operate at 45 percent. That's why we didn't recommend a higher equity ratio, even though it's lower than the US peers

because it's still higher than its Canadian peers and in our view, that's appropriate because it is a different risk profile than its Canadian peers, so we therefore just relied on the ROE model results without making any adjustment for the fact that Newfoundland Power had a lower equity ratio than the proxy companies because it has worked, the company continues to raise capital on reasonable terms, as we understand it, and we think, we understand it's, from a company perspective, it has worked well and we think it's justified by the data.

CHAIR:

Q. So I was looking at the Alberta case where, I guess the new ROE came out to be 9 percent, I think, the AUC was –

MR. COYNE:

A. It's currently—9 percent was the base and then it's adjusted once since then for the new market data and I believe it's 9.288 percent currently.

CHAIR:

Q. Okay, but the capital structure in the

Alberta utility, I think, is 37 percent, is it?

MR. COYNE:

A. 37 percent, yes. And the rationale that that board articulates around that is that Alberta's utilities are T&D only utilities, both on the gas side and on the electric side and therefore, they consider them to be at the lower end of the risk spectrum.

CHAIR:

Q. Could you just discuss that a little bit because, I mean, I kind of view Newfoundland Power as closer to a transmission, distribution utility because it only has a small amount of generation, so I've struggled in thinking about Alberta with only 37 percent equity versus the 45 here, and is it the stronger economy or there's probably a lot of factors, but if you could just comment on that it would be helpful.

MR. COYNE:

A. Sure, from the board's perspective in Alberta or ours or both?

CHAIR:

Q. More just from—okay, your perspective to

start.

MR. COYNE:

A. Yeah, well we recommended a higher equity ratio than that in Alberta, but as did some other experts, but the view of the board was because they don't have that supply function at all, as opposed to Newfoundland Power which does have supply responsibility, they're relying on Hydro for 93 percent of its energy, that they still have the responsibility of making sure that they have enough power to meet their customers needs. In Alberta, they rely on other retail providers who are responsible for providing energy to those customers, so they are purely T&D companies. In Ontario you also have pure T&D companies and there those electric utilities are at 40 percent, you know, so just nominally higher. As we compare Canadian companies to their US peers that are 50 percent, 52 percent, in that range, we see that as a gap over time that ultimately places Canadian utilities at greater financial risk or at least their investors at greater financial risk, so we

think over time, given integration of capital markets, it makes sense to look for closure there, you know. We have not recommended parody, that these equity ratios need to be exactly the same, but we're in the middle of a process in Ontario that's reconsidering where those equity ratios should be and in my mind, I think Newfoundland is probably setting a good example, you know, for something that's a middle ground between where Canadian utilities typically have been, where we think they need to be in order to continue to raise capital on a competitive basis.

(12:15 p.m.)

CHAIR:

Q. Would one aspect of it be a difference between Alberta and Newfoundland is the fact that the pricing for the distribution and transmission utilities is unbundled in Alberta versus bundled in Newfoundland and Labrador, so from a volume variance forecast perspective, so if sales vary, then Newfoundland Power experiences the impact of volume decline on recovery of, let's say,

distribution costs, whereas in Alberta they wouldn't have that volume risk as such with regard to the pricing, would that come into play in evaluating the business risk in looking at one versus the other?

MR. COYNE:

A. It does and that's a good synopsis. You know, here it is bundled and there it is unbundled, so it's separated the risk of the generation supply function away from those utilities.

CHAIR:

Q. I have one last item. It was mentioned earlier with regard to the rate mitigation plan of the government, the press release hasn't been fully clear on how it will all work, okay, so it wouldn't be difficult for someone to misunderstand how it will actually work and I'm sure there's lot of speculation on how it's going to work, but if Hydro was using its non reg profits to effectively fund the Muskrat Falls costs, so it wasn't going into a deferral account to be ultimately be recovered from customers, would it have any—how would that impact your opinion with regard to whether this is just pushing the issue forward or not?

MR. COYNE:

A. It is and I went back and looked at that after our discussion to make sure that I understood it and now I realize that I don't fully understand it either because there's some ambiguity between what's said in the press release and what's said in the slide deck that accompanied the press release. Now I'm less sure about exactly how that would flow through rates. On the issue of whether or not it's deferred or foregone, I think there's probably some ambiguity there, but if you're trying to recover the cost of a 13.5 billion dollar investment, if you are foregoing to the first premise that Hydro might forego those earnings entirely, there's two pieces of rate recovery from an asset like this and one would be depreciation over that period of time, and the other would be a return on its capital. And in a typical deferral, you would take anything that is not the cost of service and that would be depreciation plus your return

on investment and you would place it into a deferral account and you might earn something on that deferral or you might not or you might earn a debt return and then you'd recover that at a later date. So it's not clear to me based on what's been provided in the public domain exactly how that would work. If it's foregone or will be deferred and how that, if it would be deterred from a rate standpoint, if it would be recovered in a future date, but to your basic question, though, if it were foregone entirely and not to be recovered, then I'm not sure what that reduction is on the overall cost of the 13.5 billion dollars, but I assume it's relatively minor share of what that would be over the life of the asset.

CHAIR:

Q. So your view is that the cliff is still high once you get beyond 2030, even if there was internal funding offsetting the cost of Muskrat until that time?

MR. COYNE:

A. Oh yes, yeah, because my assumption is—and I

say it's an assumption, that would be recovering those costs, typically for a hydro electric asset and these transmission lines, those are probably 50 year assets and as a result of that, if you're foregoing depreciation for the first five years, you still have 45 years left to recover and then you have your rate of return. As you're depreciating that asset for those remaining 45 years, so on just a simple math basis, 5 out of 50 without knowing the exact figures, would be, I guess, would that be 10 percent of the total costs that would be foregone on a 13.5 billion dollar asset, so I think it's still a significant economic issue for the province to resolve.

CHAIR:

Q. So it wouldn't change any of your recommendations in your evidence?

MR. COYNE:

A. No, and I think the other thing is, you know, from an investor standpoint as they would look at this, we have uncertainty about exactly what the government is doing to try and mitigate it based on what's been

said and so investors would be looking at it the same way. As we have cited in the credit rating reports, it's a problem that still remains to be solved and we don't yet have full clarity about what that solution is.

CHAIR:

Q. All right, thank you.

MR. COYNE:

A. You're welcome.

MR. O'BRIEN:

Q. Nothing arising, Mr. Chair.

MS. GLYNN:

Q. I think if we could take a quick five-minute break to switch over the witnesses.

CHAIR:

Q. Okay, thank you.

(BREAK - 12:21 p.m.)

(RESUME - 12:23 p.m.)

CHAIR:

Q. Any preliminary matters Ms. Glynn?

MS. GLYNN:

Q. Yes, Mr. Chair, I believe that Newfoundland Power has a preliminary matter to raise.

MR. O'BRIEN:

Q. Yes, Mr. Chair, and I think you're aware that the issue, Dr. Booth, I understand is going to provide some direct evidence this morning by a slide show presentation which we understand will cover roughly 50 slides. I don't get the understanding if the intent is to put the presentation on the record, but it is to put the presentation up on the screen and to walk through it. I do feel the need to raise an objection and then I do think this will take quite a long time and it does amount to largely a review of a report that's on the record. I think the parties have the ability to question Dr. Booth if they are uncertain about portions of his report and that's what the normal process has been, so I'm a bit concerned about the time this will take and whether or not this is additional evidence that will be put on the record. I'm assured it's not additional evidence, but I don't know how the discussion the slides will go, so I do feel I have to raise an objection at this point.

(12:30 p.m.)

CHAIR:

Q. Yeah, well it is a bit unusual, I except with regard—sorry, I'll let Mr. Browne speak first. Mr. Coffey, sorry.

COFFEY, KC:

Q. Thank you, Mr. Fagan. This is simply a means of presentation. The last time Dr. Booth testified here, his opening statement was an hour and 17 minutes and I've looked, I did the calculation. Here, I think it's important, members of the Board, that although the evidence has been filed, the summary of it be available, and provided by the Consumer Advocate's expert in this regard. There are many, as you've heard, many, many millions of dollars involved in this. This is a very important topic and, you know, from my perspective, as counsel to the Consumer Advocate, you know, an option would be to simply keep going back and forth to various pages in his report and the appendices and so on, instead of—and that is disjointing when you're presenting something. It's far easier to see something just brought up, it's there, it's already

there. I understand from Dr. Booth that there is one, an updated piece of information in one of the slides because of something that happened, became public a week ago, a technical matter, and there is one other slide, I understand slide 3, that it's not in his actual report but there's already a reference here and in fact, it's a matter that was before this Board years ago back in 2016, it's just one comment. So it's a matter of presentation and manner of doing it. I am, my background doesn't much matter in this, but I'll make the comment anyway, that I am very familiar with presenting matters in front of tribunals and courts and it's my belief that rather than, in terms of being able to make this comprehensible, it's my belief that having something to look at visually and listening to the witness testify in relation to what you see in front of you, makes it far more comprehensible for the person who is actually listening and watching, than it does just simply hearing somebody talk. So this is an aid to comprehension, it's a

modern method and it's used in all sundry aspects of life. So that is our position, it's, the amount of time we spent, in fact frankly, we spent more time talking about this between—not in front of you, but between ourselves, the lawyers and stuff, as much time probably in total as we would have done in just doing it. And as a matter of here, when you look back at the 2016 opening statement by Dr. Booth, and it was done with, I understand, no objection. You know, it was detailed. There was no objection made and here, rather than just simply winding up with a question, you know, two or three questions and have him repeat what is in effect read off an answer, which in fact I watch – I witnessed here, and you know, that's happened, rather than have that, it's a matter of having it visually there and you can listen to him and I am hoping that it will convey to you in a more comprehensive way what it is he's trying to communicate. So, that's really – it's different, but I think it is more – it would be more effective, as an advocate.

CHAIRMAN:
Q. Well, in this circumstance –
MS. GLYNN:
Q. Mr. Chair, if I could add, please?
CHAIRMAN:
Q. Oh, that would help, yes. I apologize.
MS. GLYNN:
Q. I think we have three issues here that needed to be addressed. One was a misunderstanding of how the presentation was going to be recorded by the Board. We have worked that out between counsel that it will not be added to the record. As Mr. Coffey just indicated, it is an aid for Dr. Booth to be able to present his evidence. So, we have worked that particular issue out.
The second issue is if there is new evidence that will be presented in this presentation by Dr. Booth, as Mr. O'Brien pointed out, we will address that as the presentation goes on. If there is new evidence, Mr. O'Brien can certainly speak to that at that time.
And then there is the timing issue. As Mr. Coffey pointed out, yes, the direct

testimony of Dr. Booth was longer than most other witnesses last time. That's to be expected with the information that we're given, and if that is the way that the Consumer Advocate wants to present this evidence, we will give him the time that he needs. I do recognize that we are in a bit of a time crunch here today for 1:30. So, I'm hopeful that we might be able to get through Dr. Booth and his direct testimony today.
CHAIRMAN:
Q. Yeah, I mean, to me it's the, well it's the largest issue in the hearing; at least one of the top two. And there's only two cost of capital experts, and so, there's one representing the Consumer Advocate, so I think, you know, we really need to let him present his case, but hopefully in the most efficient way we can and move it along and certainly follow the guidelines that Ms. Glynn mentioned. So, we'll proceed. Thank you.
DR. LAURENCE BOOTH, SWORN, EXAMINATION-IN-CHIEF BY BERNARD COFFEY, KC

COFFEY, KC:
Q. Would you, for the record, please state your name?
DR. BOOTH:
A. My name is Laurence David Booth.
COFFEY, KC:
Q. And you're referred to as Dr. Booth in your professional life?
DR. BOOTH:
A. To a lot of things, but Dr. Booth, I'm perfectly comfortable with.
COFFEY, KC:
Q. And Dr. Booth, you filed a report in this, in relation to this proceeding?
DR. BOOTH:
A. Yes, I did.
COFFEY, KC:
Q. And do you adopt that as your evidence?
DR. BOOTH:
A. I do.
COFFEY, KC:
Q. And that report includes your CV itself?
DR. BOOTH:
A. It does.
COFFEY, KC:

Q. It does, yes. And I'm not going to take – again, that's there to be read by the Board. Dr. Booth, we have a slide presentation I understand you prepared. Ms. Bown, I believe, has control of the slides. So, I'm going to ask that you utilize the slide deck to give an overview to the Board of your position concerning the cost of capital.
DR. BOOTH:
A. Do you want me to refer to the pages in my testimony that these slides are derived from?
COFFEY, KC:
Q. No, in relation to that, I would just suggest this: is that no, there's no need to do that. If it turns out that – one could actually go afterward and look, but no, you go ahead. Just this is an aid to your presentation. So, obviously the first page of the slide deck is what this is about. Newfoundland Power, fair return and capital structure. So, you go ahead, Doctor.
DR. BOOTH:
A. Next slide. And I hope Mr. O'Brien doesn't object too much to some of my comments, but

this is a critical issue, what is the legal standard in Canada and the United States. And several times I heard Mr. Coyne yesterday refer to alternative investments and alternative allowed rates of return. That is not the standard in Canada. The standard in Canada is that of Mr. Justice Lamont and the definition states, "the company will be allowed as large a return on the capital invested in the enterprise as it would receive if it were investing the same amount in other securities possessing and attractiveness, stability and certainty equal to that of the company's enterprise". So, the front and foremost is risk and I'll be talking about risk. But there's also something in there which is relevant to Canada but doesn't seem to be as directly relevant in the United States. That is it specifically refers to securities. It doesn't say investments. It doesn't say alternative business investments or rates of return that firms earn elsewhere. It refers to securities, and there's a big difference between the rate of return on a security and

the rate of return earned on a business.

And yesterday, I was struck, and I talked to this with counsel before, on Emera's sale of the stake in Labrador Island Link. Now, my understanding from the news release is that the book value of that investment is 750 million dollars. KKR is paying 957 million dollars for that 750 million dollars in book value and agreeing to take over Emera's commitment to the 135 – whatever it is, 300 and so further commitments. Now, it's important to understand the book value of that investment is earning at 8.5 percent. That is not KKR's required rate of return. It's not their fair rate of return. It's not the rate of return that you get on securities of equivalent risk. The securities that it's buying is the equity stake in LLI (sic) and it's paying a 207-million-dollar premium to buy that 750 million dollars in book value. That 270 million – 207 million dollars earns a zero rate of return, zero rate of return. KKR is spending 207 million dollars just to get the 750 million dollars earning 8.5

percent. That happens all the time in the flipping and the sale of regulated assets. The AUC has looked to that in terms of its recommendations because it directly measures what is the rate of return on alternative securities with the same risk, which is the legal standard in Canada.

If you take into account the 207 million dollars that's earning zero, KKR's actual required rate of return or fair rate of return is way less than 8.5 percent. It's market to book ratio, which is the 957 million dollars its spending divided by the book value, 750 million dollars, is about 1.28. And we look at the market to book ratio to assess whether the fair – the rate of return is fair. That is standard across every regulator and textbook that I've looked at. 1.28 indicates that the allowed rate of return of 8.5 percent on the Labrador Island Link is excessive. The fact that they're paying a premium for it indicates it's excessive. KKR are not stupid investors. So, the actual fair rate of return that KKR wants is less than 8.5

percent. If you assume all they expect to get is 8.5 percent, their fair rate of return is about 6.6 percent, 6.7 percent.

MR. O'BRIEN:

Q. Mr. Chair, I'm going to have to take Mr. or Dr. Booth up on his comment. None of this is in Dr. Booth's evidence. So, we're on the first slide and now we're talking about something that's outside of Dr. Booth's report.

CHAIRMAN:

Q. Mr. Coffey?

COFFEY, KC:

Q. Yes. Well, it – bearing in mind that the KKR and Emera and Newfoundland and Labrador Hydro announced that deal on May 28th, 2024, this year and closed it on June 4th, it could hardly have been, you know, in terms of within Dr. Booth's reports, number one. His report was filed before May 28th. That's number one. Number two, the Emera/KKR deal has been – at least what's publicly known in terms of the materials that were provided yesterday, what's publicly known is before the Board; has been before the Board at

least since yesterday. So, you know, it's – he's made the comment he has. It's certainly not in his original report because of course there was no way for it to be. It hadn't happened. It's happened and he's made a comment. If Mr. O'Brien wishes to cross-examine him on it, of course, or questions on his views on it, those questions can be put. And Mr. O'Brien's certainly correct, it's not in his report. But this has only just happened.
MR. O'BRIEN:
Q. It's not in any supplemental evidence or request to file supplemental evidence.
COFFEY, KC:
Q. Oh, it -
MR. O'BRIEN:
Q. We're talking about a press release here.
CHAIRMAN:
Q. Ms. Glynn?
MS. GLYNN:
Q. I didn't know if Mr. Coffey had any -
COFFEY, KC:
Q. No, no.
CHAIRMAN:

Q. Okay.
MS. GLYNN:
Q. Mr. O'Brien correctly points out that the rules for procedure do say that if any supplementary evidence is wanted to be provided by a witness that there should be an application for that to be made or a request for that to be put through the witness.
(12:45 p.m.)
COFFEY, KC:
Q. Well, it was put before – my understanding of that was it would be put before the Board, and it was. I filed it the day before I was going to cross-examine Mr. Coyne.
MS. GLYNN:
Q. But you didn't ask for this witness to be able to provide -
COFFEY, KC:
Q. Oh, this – oh, I apologize for that.
MR. O'BRIEN:
Q. This witness.
COFFEY, KC:
Q. It was just I thought once it was before the

Board, it's before the Board. That was my – that's – I didn't realize it had to be for each individual witness.
MR. O'BRIEN:
Q. Well, this witness is expressing an opinion now on a – an expert opinion on what is put before the Board as a press release. There's no indication Dr. Booth has reviewed documents associated with this transaction or has put himself in a position to provide a fair and objective and impartial opinion to the Board on this. Yet in our first slide here, this is what we're talking about.
COFFEY, KC:
Q. That's – they're my comments.
CHAIRMAN:
Q. Any further comment, Ms. Glynn?
MS. GLYNN:
Q. No, not at this time, Mr. Chair.
CHAIRMAN:
Q. Well, I think the -
DR. BOOTH:
A. Can I clarify, Mr. Chairman?
CHAIRMAN:

Q. Yeah, I'd like you to speak before I comment. Go ahead.
DR. BOOTH:
A. I'm just making a point about the definition of the legal standard. I can retract any comment on the Labrador Island Link, but the comment is simply that the basic definition of a fair return in Canada is based upon the securities, not on the book value of the investment. The price paid by KKR for the Labrador Island Link, all I'm saying is if it a premium -- and I don't know whether it's a premium. All I'm doing is relying upon the information that was put before the Board yesterday. If it is a premium, it means that the 8.5 percent rate of return is attractive. That is my expert opinion. That would be the opinion of any undergraduate in finance. That is not, I would suggest, a contentious issue. But the point is simply what is the legal standard of a fair return. And if you listen to Mr. Coyne yesterday and today, he consistently said fair return standard. He consistently said fails to meet the fair return standard.

And here we have an objective example directly relevant to this hearing that indicates what the fair return is. So, that would be my computation.

CHAIRMAN:
Q. I think what Mr. Booth has done with regard to a simple computation of the press release purchase value relative to the book value presented in the press release probably wouldn't be a surprise with regard to the purchase price being in excess, which would indicate the return being lower. So, I'm struggling with that being a challenging matter to ask questions on. The issue itself was brought up yesterday and so that is on the record. I think if you – Mr. O'Brien if you want to talk more about this, I think you'll have time to ask questions on it tomorrow.

MR. O'BRIEN:
Q. That's fine, Mr. Chair. Just I didn't know how far we're going down this road and we're on the first slide.

CHAIRMAN:
Q. Yes, yeah.

MR. O'BRIEN:
Q. And this is a significant discussion on something that's not on the record from Dr. Booth.

CHAIRMAN:
Q. Yeah. I think the –

MS. GLYNN:
Q. And I think the reminder of the direct testimony to bring out what is in the current report and then the parties will explore other issues, such as press releases or any other information items that were presented throughout the testimony that we've heard in the last few days.

CHAIRMAN:
Q. Yeah. So, Dr. Booth, you know, you could – hopefully we don't have any other press releases as we proceed through, to make it easier.

DR. BOOTH:
A. And I'll be honest with you, I only – when I prepared my slides, I never ever anticipated talking about the Labrador Island Link. So, it was there to talk about risk and it was there because the legal standard means that

you have to take into account risk. So, the main way in which utility witnesses advocate higher returns is through higher risk. So, I've always referred to utility witnesses as risk generating, in the risk generating business.

CHAIRMAN:
Q. So, we'll take what you discussed about the Labrador Island Link as an illustrative example of your point, and then we can just move on.

DR. BOOTH:
A. Yeah, I was just going to say take company A with a 750 million book value and company B, but I couldn't resist, I'm afraid. So, next slide please. So, risk, in 2016, I referred to all of the instances prior to then of company witnesses advocating higher risk. Mainly it was fuel competition and how that was putting the company at a disadvantage. And I was looking at the 2016 testimony and I – the difference between Mr. Coyne and I is I regard settlements as a black box. So, the only litigated was 2016. So, I went back to 2016 to see what Mr. Coyne said and

I don't have to read all of this out, but everything he's saying today, he said in 2016, and it refers to Muskrat Falls. It refers to the reliability of the power. It refers to the small – nothing that he said today in his testimony is any different from 2016.

Turn over. One thing that is dramatically different between Mr. Coyne and myself is that I've been testifying in Canada since 1985 and I first testified before Bell Canada, before the CRTC on Bell Canada. Bell Canada went through dramatic changes in its risk. Trans Canada, in 2012 I think it was, faced dramatic changes in risk. So, the history in Canada has been that we do not standby and let utilities hang out to dry. This is what I said in 2004 before the Trans Canada – before the National Energy Board. It was to do with a hearing – and this is on my testimony, page 92. This was to do with a new pipeline we were putting in down MacKenzie Valley and Perry were proposing it and the NEB had to look at all of the cash flow predictions out

25 years. But they only had signed contracts to lease for the gas to run down the pipeline out for a shorter time period. So, the question was what happens when those leases run out, and that was where we started talking about short-term versus long-term. And I said then, and I still hold to this, it's what I view as the regulatory compact in Canada. If problems occur, then firms bring these problems to the regulator and frequently compromises are worked out. This is part of the regulatory bargain that I now refer to as the regulatory compact. Only regulated firms have this capability. For example, if a competitive firm suffers a supply shock, then the stockholders are directly affected. But in contract, a regulated firm can, that have losses, put in a deferral account and allocate it to future customers or apply to the regulator for other means to protecting the stockholder from loss. Consequently, it is unreasonable to expect no action on the part of the regulator to the increased risk after year 11, and year 11 was when these –

the contracts on the MacKenzie Valley pipeline ran out. I still hold to that.

I believe that you commissioners are reasonable people and I believe that every board across Canada has got reasonable people and we look at our utilities and we protect our utilities. I've never seen an instance when a utility wasn't protected in Canada, and that's part of who we are in Canada. We don't hold the utilities out to dry. Now, next slide please.

So, how can I verify that? Every hearing I've been involved in, at least for the last 25 years, I've asked for all the evidence on the allowed rate of return and the actual rate of return, and for Newfoundland Power, last 30 years, it's over earned its allowed ROE, and I ask what happened in the early '90s. That was when it was competition from fuels, and they said no, it was a CRA audit, and they had to lose money on an audit and then they got the money back on audit. And Mr. Kelly and I went through this in 2016 and he said also it was due to the cod problem at that time,

which I can't say whether it was or it wasn't, but for 30 years, Newfoundland Power has consistently earned its allowed ROE. Now, that is not at all unusual in Canada. Practically every utility I look at, they do that. And why? Because we have deferral accounts to pass on most of the risks to ratepayers and that's the most important thing. I constantly hear utility witnesses say, "risk, risk, risk. The sky is falling. There's increased risk." It's not really utility risk. It's ratepayer risk because the way we operate in Canada is those risks are passed on to ratepayers. It's ratepayers who are going to pay the cost of higher electricity prices, and I'll talk about that on the next slide, and I'll skip a lot of slides in my testimony because the question is Mr. Kelly in 2016 said, "well suppose prices go up 50 percent" and that was the prevailing opinion at that point. Now, risk mitigation, they're not going up by 50 percent. They're going up by 2.25 percent possibly. And then the question is, which utility witnesses never addressed and

I've never seen utility witnesses put in the allowable as actual. That's always me that has to ask for that. They prefer qualitative assessments. But the question is: what electricity prices in Newfoundland will cause a risk to Newfoundland Power? Nobody wants to pay more for electricity, but what's the capacity to increase electricity prices in Newfoundland?

And Hydro Quebec puts this table together every year and it's exactly the same table that I presented in 2016. The lowest cost producer is Quebec. Apart from their own power, they've got Churchill Falls coming through, which is at a cheap rate. So, they've got very low-cost power in Quebec. Vancouver and Winnipeg also have huge reserves of power. So, they've got low-cost power. And then you look at the next one, Ontario or Ottawa, sorry, and then St. John's. I hate to tell you guys, but you're not paying a lot of money for electricity. If you go to Halifax, they're paying – well, if you drop down here to Halifax, where is it? $234 for the same amount of power. And we had a big hearing last year about their coal plants. They're going to be put in a deferral account and they're going to be paying twice for electricity. So, they're going to be bump up in electricity costs in Nova Scotia because they're still going to be paying for those coal plants that are no longer used and useful. And then we look at Prince Edward Island, where I can't find – oh, there's Charlottetown, PEI at 228, way higher than in St. John's.

So, the question is how high can electricity prices go in St. John's and in Newfoundland before people start going to alternative means of heating. And what are the alternative means of heating? We got carbon taxes that are currently at $80 a ton going to $160 a ton. So, I find it extremely difficult to believe that anybody right now, if electricity prices go up in St. John's, they're going to basically decide to go to home heating with heating oil given all of the increases that are going to come down the pipe for home heating

oil. So, the question is not just are electricity prices going up. I don't know what they're going to go up, but the question is how high can they go, and are people going to stop using electricity because of that, and I just don't see it happening.

My daughter lives in New York, in Brooklyn. She is paying as much – and sorry, this isn't in testimony. Counsel told me to cut it out. I shouldn't refer to my family. But she's in Brooklyn. She's paying more to heat a two-bedroom condo in Brooklyn than I pay for a five-bedroom house in Toronto. So, Canadians don't realize how lucky they are in terms of the power cost. So, she's not cutting the cord, which usually refers to cable, but the power cord, and even if she did, how are we going to be using our televisions and all sorts of things, and computers and stuff? We need electricity. So, that's my comment on the long-run risk.

Importance of business risk, business risk is at the core of the common equity

ratio. The National Energy Board -- next slide please, in my testimony page 89, you know – well, perhaps one – can we go back to the one – oh, same slide. Forget about that one. That ones seems to have dropped out of the slide deck.

Business risk is the main component of determining the capital structure. The National Energy Board and the Ontario Energy Board and the BCUC basically look at business risk before they determine common equity ratio. The basic principle is you don't add a lot of financial risk on top of business risk. And in order to equalize to use the same allowable rate of return on oil pipelines versus gas pipelines in the NEB case or gas versus an electric utility in Alberta, you need to equalize the risk. So, first of all, you equalize based upon the business risk with the common equity ratio. Then you give them all exactly the same allowed ROE. So, sometimes they look at it and say, well, you know, Dr. Booth says they're all equivalent in risk. Well, that's the way we tend to do it for multiple

hearings. We basically equalize the risk and common equity ratios, equalize the business risk, then give them all a generic ROE.

(1:00 p.m.)

The Alberta Utility Commission calls it a generic ROE and so that's the importance of business risk. So, next slide please. Oh, can I go back two slides? The Canadian comparators. And the one before that. Oh, we seem to have dropped that one out. Okay.

Canadian comparators. This is directly from – and I was trying to slim the slide deck out. The direct comparators for Newfoundland Power are the other Fortis electric companies. So, rather than going to Duke Energy or going to American Electric Power, and I'll talk about those, what about the other Fortis electric utilities? What about Fortis Alberta? What about Fortis Ontario? What about Maritime Electric? And I don't know why they don't call it Fortis PEI, but what about – and what about the old West Kootenay Power in BC, Fortis BC Electric. They have 37-40, 40-41 percent common equity ratios. Nova Scotia Power, I was in a hearing two years ago. It was 37.5 percent. By settlement, we agreed on 40 percent because it's facing significant problems and because the province intervened in the middle of that hearing. There's absolutely no question Newfoundland Power's 45 percent is out of line. I've been saying that ever since I've been coming here, I think, since 2009. The Board has not made any changes because it's always sort of said something like, "well, Muskrat Falls is coming along. Let's wait and see". I'm not pushing hard on 45 percent – sorry, 40 percent. What I'm saying is go back and put in the PUB's decision in '96/97 a range of 40 to 45 percent. So, the bond rating agencies know that it's 40 to 45 percent and if you want to go to 40 percent, I will recommend you go immediately. Even then I've been I think quite conservative saying go slowly, a little bit over time. Add preferred shares. Don't shock the market. But recognize that 45 percent is excessive compared to the Canadian comparators.

So, when we look at other comparators -- next slide please – Mr. Coyne goes to the United States. Now, I've got to be careful what I say that's not in my testimony, but there aren't many Canadian witnesses out there. When I started testifying, most of the witnesses in Canada were Canadian. After we signed the free trade agreement with the Americans in 1987, I started shopping in Costco instead of other stores. I started shopping at Home Depot instead of Aikenheads. I started shopping at Business Depot. There's absolutely no question that we've become more integrated with the United States ever since the Free Trade Agreement. That does not mean to say that just because we're more integrated that we can take US companies without adjustments into Canada, and that's the critical thing.

I look at US companies now. I never used to. When I started out, I looked only at Canadian companies and I've got an exhibit somewhere where I looked at the companies that I used to look at. My first attendance here in Newfoundland was in 1991.

Newfoundland Tel here before the CRTC because Newfoundland Tel went from provincial to CRTC regulation. Newfoundland Tel doesn't exist anymore. New Brunswick Tel doesn't exist anymore. Island Telephone doesn't exist anymore. Maritime Electric exists but not as a private company. Consumers Gas doesn't exist as a private company. We've lost a large number of Canadian companies. So, in my testimony somewhat I'm forced to look at the United States, and that is absolutely correct, forced to look. We should be looking at Canadian companies in Canadian capital markets, but we're forced to look at the United States. But that doesn't mean to say that we take US evidence in without making adjustments and seeing whether it truly is comparable.

Now, in terms of Mr. Coyne's US comparators, Mr. Coffey was going to go through their 10Ks and show just how diversified they are, and how many coal plants they have and how many nuclear plants they have. And this is Mr. Coyne's

evidence. He asked me what's significant about nuclear in terms of how significant does it have to be to make sense. I should have said it depends on how many there are. You only need one of them to cause a disaster. So, to some extent, it doesn't matter how many they have. Any of them are probably exposed to more risk. And these utilities, the only one without much generation is Eversource. Of all of these US companies, the one that's closest to being a pure T&D like Newfoundland Power is Eversource. Otherwise, I find it extremely difficult to accept as comparables for Newfoundland Power companies that are integrated US utilities, which means integrated power generation, coal plants, nuclear plants, wind plants, co-gen plants, gas co-gen plants, and then a diversified group of customers, industrial customers as well as retail. There aren't anywhere close to comparable to Newfoundland Power. And previously, Mr. Coyne has made adjustments. He did this before Hydro, the Regime in Quebec, and made adjustments for Hydro

Quebec because he didn't have Hydro Quebec transmission, Hydro Quebec distribution, because they didn't have any power. All of their power was coming from Hydro Quebec, and he made an adjustment there. So, the question is how big an adjustment do you have to make to these US utilities to make them comparable to Newfoundland Power. Clearly, they're not comparable. And the problem with other regulators looking at them, it depends what the evidence that they put before them. I don't know whether in the AUC or the BCUC hearings people put all the 10Ks of Mr. Coyne's samples to basically cross-examine him on the comparability of the sample. But this Board rejected this when Tom – I've forgotten his name, the counsel.

BROWNE, KC:
Q. Tom Johnson.

COFFEY, KC:
Q. Johnson.

DR. BOOTH:
A. Tom Johnson, sorry, counsel on behalf of the Consumer Advocate. And the Board rejected

their comparability because of exactly these problems, and this hasn't changed. Duke hasn't got rid of its nuclear power plants. They're still there. So, that's a concern. Next slide please.

Where the rubber meets the road is here in the ROE. This is an exhibit I've got my – it's Schedule 9. It's got Newfoundland Power's earned rate of return over this time period and all of these electric utilities. They are not comparable even when you look at the financial data. The average earned ROE of Newfoundland Power, 8.92 percent. The average from this sample, 9.19 percent, which is less. You look at the variability and the average across these utilities, Duke Energy, I don't know how you can think Duke's comparable to Newfoundland Power. The ROE, it hasn't been above seven and a half – or sorry, 8.15 percent in basically 12 years, and it's got a lot of variability in its ROE. The variability in the ROE is a major criteria in the bond rating. The rating companies like to see very consistent regular ROE because that's what is basically

there to support the bond rating, and these are all riskier utilities by any definition. How do we look at how the market looks at that? The way at which we look at this, we look at price-to-book, or market-to-book ratios. That's basically the book value, the asset, and what is it selling for in the capital market. All of these utilities, even with their volatile ROE's relative to Newfoundland Power, are selling at price-to-book ratios significantly above about 1.1 or 1.15. Previously before this body, Kathy McShane, the witness for Foster and Associates and the company, used to say market-to-book ratio should be 1.1 or 1.15, and then now to boost the ROE to account for issue cost and things. These are well above 1.1 and 1.15, which means the market is very happy with what these integrated companies are doing.

Now, the crux. I've forgotten how many times Mr. Coyne said fair return standard, and I was intrigued by Mr. Simmons' cross-examination, because you got to remember that Kathy McShane was the company witness

until 2012 I think it was. Mr. Coyne came into Canada 2009, and before the Alberta Utility Commission--now, I give him, that's the list. He went to the Alberta Utility Commission and told them you haven't been given fair return standard ROE's, and he produces this document, and I can't verify the first three years. I don't believe for a minute they're exactly the same, but he said there's a fairness deficit. Deficit means something below, which must mean he felt that allowed ROE's in Canada were less than fair compared to what, compared to the United States.

He has consistently said since coming into Canada fair return standards, give them what my US sample gives. Treat them like American companies, and give them higher allowed rates of return, and give them more equity, and he said basically the same thing here.

So, that was his calling card coming into Canada for utilities. Hire me because--and this is obviously being factious, but basically I believe that allowed ROE's in Canada should go up. They're not meeting the fair return standard. I do not believe that for a minute. He said that it was due to the use of automatic adjustment mechanisms. That's absolutely incorrect. The Alberta Utilities Commission didn't put their utilities on an automatic adjustment mechanism until 2003. These "unfair allowed rates of return" started in '97, '98, and '99, 2000, way before the Alberta utilities went on an automatic adjustment mechanism, and I was in a hearing before the Trans Canada--before the NDP on the Trans Canada Mainline where they reviewed their automatic adjustment formula, and they said in no uncertain terms it's fair. I was also in a hearing before the Ontario Energy Board in 2004 where they reviewed their formula, and they said it's fair, there's nothing wrong with it.

So, these were decisions that the Canadian regulators made and reviewed their adjustment formulas, those that had them,

and they decided they were fair returns. Mr. Coyne has come into Canada and said what we do in Canada is not fair. I do not accept that.

So, that's an overview really of the difference between Mr. Coyne and myself. I tend to think that Canadian boards have made serious decisions after litigated hearings with significant evidence, way more evidence than they get in the United States.

I'm told, and this is hearsay evidence, that their hearings basically half an hour, or an hour, on fair ROE. They've narrowed it down to a smaller number of things that they talk about. Our decisions are much more broader. I've been involved in five days of hearings into a fair ROE.

So, then the question is, the legal standard is not just a market based opportunity cost on securities, but changes in the money market. What's going on in the capital markets? What's changed since the last litigated hearing in 2016? The core of that is the money market, the overnight

rate, and that's--Mr. Coyne didn't mention it. Well, he said integrated markets. They're integrated between the US and Canada. Absolutely no question, the money market is totally integrated.

You've tested me I'm afraid, Mr. O'Brien, but Canadian banks borrowing the US dollars, pound sterling, any currency, and they swap it into Canadian dollars. They find wherever it's cheaper. But just because it's integrated doesn't mean to say that the rates of return are the same. You hedge them. You get currency risk. You've got--you forward--you hedge it by buying forward weights to hedge the foreign currency risk, and this is the--Canadians do this--Canadian banks do this every single day. They look to where can they find the cheapest funding.

So, the money market is where we start, and when you look at this--go to the next slide please.

(1:15 p.m.)

The business cycle is critical for all

of this, and Mr. Coyne repeatedly said, well, things have increased since 2020. Well, sorry, what's that got to do with it?

2020--first of all, it was in 2016. This is the history of long Canada bond yields and treasury bills in Canada going back to 2000. Now, I must admit, I added these arrows because they're the points that are always interesting because it reflects the policies of the central bank. The Bank of Canada pushed up interest rates in 2000 to slow down the Canadian economy. That's what they do. There's lots of discussion at the moment about how young people are really hit with mortgage costs. It happens all the time. It's regular as clockwork. You push up interest rates, mortgage rates go up, and you slow down the economy. It happened in the early 2000's.

The T-bill rate, which was very close to the money market rate, went up to the long Canada rate, and then it brought down the rate of inflation. The Canadian economy went into recession as a result of the techs rec (phonetic) and then honky-dory, we stayed the same until 2008. 2008 Canadian economy was getting strong again. Ontario, we had high inflation. We went above the 3 percent top of the range. So the Bank of Canada pushed up the T-bill rate again. Pushed up short-term interest rates and we got a recession, huge recession. It wasn't caused by the Bank of Canada, it was caused by Big Brother in the United States.

Every single major recession has originated in the United States, not in Canada. The Great Recession was--the Great Depression, sorry, and stock market crash, was caused by the actions of the Fed and to do with utility holding companies I should mention, not by Canada. The US likes to refer to the global recession in 2009/10. We didn't have a recession in Canada, we had a short slowdown. We were out of it very, very, quickly, and we were pushing up interest rates in 2011, and I provided evidence in 2011 about increasing interest rates and we were getting back to normal,

because in Canada we were, and then we got a message from Newfoundland Power. They said, well, the Board's adjustment mechanism is giving unfair rates return, we'd like it suspended, and that was--they asked the Consumer Advocate. The Consumer Advocate asked me do I agree to the suspension of the formula, and I said I think the actual ROE is fair, but I don't think the long Canada bond rate is fair, so I agree with Newfoundland Power, and I agree to a suspension of the automatic adjustment formula. And at that point the long Canada rate had dropped dramatically in the second half of 2011.

Why they done that is because the Americans--the economy was so bad the Americans engaged in what we call bond buying. I call Operation Twist, or quantitative--massive bond purchases to drive down interest rates.

Now, this is very, very, important. It's where I disagree with Mr. Coyne, and I disagree with a lot of other witnesses. I'm

also a Charted Business Valuator, a CBV, and the basic think in valuation is what we call fair market value. It's a legal standard in Canada and the United States. So, if any of you ever get a divorce and the spouse challenges the value of your assets, a valuator has to come in and value them at fair market value. Not at what you think they're worth, but what fair market value is. Fair market value, I've got the definition in my evidence, is basically the free market where nobody is forced to buy or sell, nobody has got more information, nobody has got market power.

There is absolutely no way the long Canada bond yield has satisfied the definition of fair market value since 2011, and before this Board in 2012/13 I said, use 3.8 percent as a minimum long Canada bond yield, and I've said I would not change my recommendations because interest rates go down, because they want fair market value. I didn't think at that time, and I still don't think, that the equity markets trade

off risk and return using long Canada bond use which were ridiculously low, and Mr. Coyne sometimes says, well, Booth has had 7.5, 7.--I've had the same basic recommendation ever since 2012, because the bond market is still not fair market value, and we're getting there as I will explain, but it's not fair market value.

After the US started bond buying basically to buy long-term bonds to lower mortgage rates, so basically allow Americans to refinance their mortgages and put money into their pockets, and also incidentally to save the banks from mortgage defaults--we recovered quite quickly. Basically we were doing some recovery until the hearing in 2016 when we went into a technical recession because China basically slowed down and stopped buying resources, and then we were doing great.

2019 we started thinking, well, interest rates are going up. The economy is very strong, and then along came COVID. And 2020, which is Mr. Coyne's--seems to be his judgment about the reference point. 2020 was COVID. COVID is not anybody's reference point. COVID--we have massive--even the Bank of Canada entered (phonetic) into the bond market. We had negative real interest rates. We had bond yields incredibly low that no reasonable person would have bought them except for the fact the Bank of Canada bought about 460 billion dollars worth of Federal Government debt, and it still has 300 billion dollars worth of Federal Government debt.

My colleague was Tiff Macklem. He's now the--he was the Dean of the Rotman School. He's now the Governor of the Bank of Canada. He admits that the Bank of Canada made a mistake. The mistake--and also every central bank made that mistake so Tiff really wasn't to blame, but COVID--I say we're living in--we've got the hangover from COVID, which is what we have.

Federal Government has doubled the Federal Government debt, doubled. It's concerned about inter-generational fairness,

but it's leaving a lot of debt for our children and our grandchildren. It's doubled the Federal debt, massive fiscal stimulus to boost the economy, and we couldn't spend the money. The savings rate in Canada went up through the roof, the highest savings rate in G7. We couldn't go out dining. We couldn't travel. We couldn't do anything, so we basically bought houses and we saved, and then as soon as we could when COVID passed we spent money.

Now, my son smashed up our car in 2022, so I had to go and buy a new car. I got more from the insurance company for compensation for my car than I paid for my car earlier because there were no new cars to buy because there was a shortage of chips, there were still supply shortages. Prices went up, and the graph is from the budget book of the Government of Canada, and this is the deviation of the inflation rate from the target. We're below trend, or below target, throughout 2020, and then we started recovering, and Tiff was very slow

on basically taking up--upsetting measurements, but we started getting all this inflation building up because we could now spend a lot of the savings that collectively we had in Canada where there wasn't much to buy.

Now, on top of that the Federal Government has made a number of very big policy mistakes, one of it was increasing immigration, and I'm not talking about a little bit, but we generally let in 250,000, 300,000, people into Canada every year. 2021/2022 we let in 1.2 million people, and surprise, surprise, those people need a house, they need somewhere to stay, and no, absolutely no planning went into providing housing for all of the recent immigrants that have come into Canada. So, surprise, surprise, rents have gone up. Surprise, surprise, housing prices have gone up, and surprise, surprise, that is a big component of the consumer price index.

So, we're living with inflation. The Bank of Canada has increased interest rates

dramatically. This--I don't' know whether this was in my testimony, but this is the reduction and overnight rate for 5 percent to 4.75 percent. We're way ahead of the United States in getting a grip on inflation.

One thing about Mr. Coyne is I never know when he's talking about--when he says something whether he was talking about the US or Canada. He did make a comment about inflation being protracted in the United States. It is not in Canada. Our economy is a lot more sensitive to interest rates, mainly because of the way in which we look at the mortgage market, but the result is that our people have suffered a lot more because of higher interest rates, and inflation has come down a lot more.

So, we're at 2.7 percent. The core measures that we look at--we take our energy because it's volatile. We also take out housing because that's caused by the Bank of Canada, and then we look at what are the capital markets believe. Now, one thing that really bugs me about Mr. Coyne and what he says, he says we'll boost judgment, judgment, judgment, judgment, fair return standard. My testimony is littered with evidence.

If I were to tell my students--when I asked them about long run inflation in Canada, I say it's two percent. Why is that? It's because the Government of Canada and the Bank of Canada committed to two percent inflation 25 years ago, and hell and high weather the Bank of Canada is not going to let the rate of inflation go up indefinitely and it's bringing it down to two percent. Do the capital markets believe them? Well, we look at what we call the break even inflation rate. It's the difference between the real return bond that gives you compensation for inflation and the nominal bond that doesn't. So, if you really think that inflation is going to be very high, you buy the real return bond and then it's indexed to inflation. To draw a line straight across the two percent you'll

see that it goes up and down, but basically two percent is what the capital markets think is the long run rate of inflation.

So, I tell my students, if I give you any question and you say anything other than two percent for the long run rate of inflation, then you'll get enough because that is that is the commitment it made in Canada. The United States has not made that commitment. So, when you talk about the US versus Canada, the US has got a commitment to two percent averaged over the business cycle which allows them to go up and to go down. We don't have that. We have two percent. So, that's the two percent rate of inflation.

I think it was Hydro asked me about independent forecasts. The PBO, Parliamentary Budget Office, basically audits the Federal Government, and they are our watchdog as they were, and they get the views of economists. This is their forecast as of February/March, which is pretty much bang-on when I was doing my testimony.

What's their forecast? If you look at inflation, 2024 it's going to come down to 2.4 percent because it's going to drop through the year. They said the end of the year. 2025, 1.9; 2026 to 2028, 1.9 percent. Nobody in Canada believes the rate of inflation of a long run is going to be anything other than two percent if they know about the agreement between the Government of Canada and the Bank of Canada.

Where's the economy? Well, we hear a lot about Newfoundland, temporary problems. Canada has it. We're in a slowdown, there's no question about that. That's why we got high interest rates, is to bring down the rate of inflation. 2024, GDP .8 percent; 2025, 2.4, and then back to long run trend about 2.1 percent. So, basically 2025, the beginning of the next cycle for the test year, basically back to normal. COVID, the hangover will be gone.

In terms of the PBO forecast on interest rates, a lot of the people use 10 year--the forecast for the 10 year bond.

Why? Because every country has a 10 year bond, and these are basically used for comparisons around the world. Every country does not have the ability to issue 50 year bonds, which is what the Government of Canada has been able to do. So, if you try to do a comparison to 50 year bonds, you can't do it because a lot of countries don't issue 50 year bonds. So, it's a 10 year bond forecast. What does he have? 3.3 to 3.4 percent. If you add--by that time the normal markets you should be adding a normal spread to the 30 year bond. That's 30 to 25 percent. You're basically at my trigger of 3.8 percent. So, for the last 12 years I've told people don't change the allowed ROE unless the bond yield gets above 3.8 percent, and I've stuck with that with my forecasts, and surprise, surprise, the BCUC just stuck with their forecast and they use 3.8 percent, and they use 3.8 percent when they adopted my suggested formula back in 2013. And I suggested that this Board use 3.8 percent, which they did back in I think it was 2013. That I think is the lowest (unintelligible) interest rate that satisfies fair market value.

So, when Mr. Coyne says, well, interest rates have gone up since 2020. Well, they have. It doesn't affect my forecast because from one suboptimal rate to another rate that's a little bit suboptimal, neither of which I've used in my own estimates or recommendations to the Board.

(1:30 p.m.)

RBC, I've been using RBC because I'm a RBC client and I get all their forecasts. I get a huge amount of stuff from RBC. It happens to be a G-SIB, Globally Systemically Important Bank, one of two in Canada, and that's a big change. Ten years ago we didn't have any Globally Systemically Important Banks. Now we have a financial system that is globally important. RBC has a long Canada bond yield at 3.15 out to the end of the 2025. Normally they're optimistic, and I'm surprised that they're pessimistic in terms of the long Canada bond

yield, and they're out of line with the other forecasters, but I'll draw your attention to the difference in the interest rates in the US and Canada.

Canada has lower interest rates than the United States. We have had lower interest rates since John Chretian and Paul Martin balanced the books in Canada and we no longer had huge deficits basically borrowing money forcing up interest rates. Canada moved to a surplus, and we ended up with lower interest rates than the United States. The US debt to GDP is well above Canada, and they've got more problems.

Now, you might look at that and say, well, Mr. Coyne says the markets are integrated. They're not integrated, or they're integrated, but that doesn't mean to say the interest rates are the same. As I said, you can take an integrated market, and if there are different interest rates, the forward currency depreciation upsets that.

So, what's happening in Canada? The Canadian dollar is gone down. Why has the

Canadian dollar gone down? Because our interest rates have dropped 25 basis point. You ask me where the Canadian dollar is going to go. I was going to say it's going to go down even more. Why? Because we are going to be lowering interest rates before the United States, and as a result we're going to--the currency is going to take the hit.

It's a basic rule in finance that I told the Board in 2016 and previously. Integration doesn't mean to say the rates of return are the same. We definitely have an integrated money market, and even the bond market is pretty well integrated, but interest rates aren't the same. So, taking interest rates--taking an allowed rate of return for the United States into Canada without adjusting for the fact that interest rates in Canada, the base for any risk premium of 125 basis points lower than in the United States doesn't make any sense.

MS. GLYNN:
Q. Mr. Chair, I do note that it's past the 1:30

timeline, just barely, and I don't think we're even halfway through the reduced slide presentation deck.

DR. BOOTH:
A. Okay. The other slides, long-term credit spreads, just to check, is the default risk in the credit markets the same? Basically the same as eight years ago. Credit spreads in the bank loan offices, basically the same as eight years ago. The volatility index, basically the same as eight years ago. Canada Financial Stress Index, the same as eight years ago.

CHAIR:
Q. I just have to ask this question of how long for the--longer you think you'll be?

DR. BOOTH:
A. I'm trying to go through these as quickly as possible. They're just basically--I will guarantee less than--less than 25 minutes.

COFFEY, KC:
Q. So, I would suggest we pick it up again tomorrow. That's just my suggestion. I can sit--I have nothing else to do. I can be

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here all afternoon, but I'll leave that to
the Board obviously.
CHAIR:
Q. We'll start again in the morning.
COFFEY, KC:
Q. Great. Thank you.
Upon conclusion at 1:34 p.m.

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CERTIFICATE

I, Judy Moss, hereby certify that the foregoing is a true and correct transcript of hearing in the matter of Newfoundland Power Inc. 2025-2026 General Rate Application heard on June 19th, 2024 before the Newfoundland and Labrador Board of Commissioners of Public Utilities, 120 Torbay Road, St. John's, Newfoundland and Labrador and was transcribed by me to the best of my ability by means of a sound apparatus.

Dated at St. John's, Newfoundland and Labrador this 19th day of June, 2024

Judy Moss

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