

## Michael Gorman's Responses to Dr. Paul R. Carpenter

**1. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, Appendix A

**Demande : 1.1** Please provide the following information related to Mr. Gorman's testimonial experience with respect to cost of capital:

- a. Regulatory body/venue
- b. Docket number or other identifying reference
- c. Party on whose behalf Mr. Gorman was testifying
- d. Utility or company for which cost of capital was being determined
- e. Mr. Gorman's recommended return on equity and capital structure
- f. Final outcome (whether decision or settlement) with respect to return on equity and capital structure of the utility involved
- g. In each case please indicate whether Mr. Gorman provided evidence on business risk for the utility involved, and if so please provide a copy of such evidence.
- h. A copy of Mr. Gorman's testimony in each matter
- i. Has Mr. Gorman's firm, Brubaker and Associates, or any of its principals ever sponsored testimony on cost of capital on behalf of a utility client? If so, please provide responses to the eight questions above for each piece of testimony by a Brubaker principal.

### **Response 1.1**

- a. Please see Carpenter Attachment 1.1 for a list of all rate of return testimony Mr. Gorman has filed in the last 10 years.
- b. Please see Carpenter Attachment 1.1 for a list of all rate of return testimony Mr. Gorman has filed in the last 10 years.
- c. Please see Carpenter Attachment 1.1 for a list of all rate of return testimony Mr. Gorman has filed in the last 10 years.
- d. Please see Carpenter Attachment 1.1 for a list of all rate of return testimony Mr. Gorman has filed in the last 10 years.
- e. Mr. Gorman has not tabulated his proposed return on equity and capital structure recommendations. This data is available in the testimony which is in the public domain.
- f. Mr. Gorman has not compiled the requested final outcome data.

- g. Mr. Gorman evaluated the total investment risk of the utility in his rate of return analysis. Mr. Gorman's testimony is in the public domain.
- h. This information is voluminous and is available in the public domain, or can be viewed, by appointment, at BAI's St. Louis office.
- i. No.

**2. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, Exhibits MPG-1 through MPG-6

**Demande : 2.1** Please provide electronic versions (in MS Excel or a comparable electronic format) of Exhibits MPG-1 – MPG-6 appended to Mr. Gorman’s testimony. Include all underlying data and calculations associated with these schedules with sources clearly noted and all formulas included.

**Response 2.1**

Please see Carpenter Attachment 2.1a and Carpenter Attachment 2.1b. Please see Carpenter Attachment 2.1c, which includes the supporting workpapers from *Value Line* and Thomson Financial, and Carpenter Attachment 2.1d, which includes the *Blue Chip Economic Indicators* as of March 10, 2009.

**3. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, Table 3 at page 27

**Demandes : 3.1** Please confirm that the credit ratings shown in Table 3 for the five Canadian utilities are credit ratings for the consolidated entity in each case.

**Response 3.1**

Mr. Gorman confirms with one exception. The S&P credit rating for TransCanada Corp. is the credit rating for its major subsidiary, TransCanada Pipeline. Please refer to Carpenter Attachment 3.1, for bond rating information by subsidiary.

**3.2** For each Canadian utility listed in Table 3, please provide the proportion of the consolidated entity's revenues, asset base and earnings (for the most recent year available) that is associated with the entity's regulated operations.

**Response 3.2**

Mr. Gorman has not compiled all of the requested data. Please see Carpenter Attachment 3.2 for compilation of EBIT breakout for each company on a regulated and non-regulated basis.

**3.3** Is it Mr. Gorman's testimony that the business risk of the regulated businesses associated with each of the five Canadian utilities in Table 3 is the same as the business risk of each entity's unregulated businesses? If not, what is Mr. Gorman's opinion (and the evidence on which he bases his opinion) regarding the differences in business risk between the regulated and unregulated business for each of the five Canadian utilities?

**Response 3.3**

Mr. Gorman has not conducted a study of the business risk of the regulated and non-regulated companies for the Canadian utilities listed in this Table 3. Generally, Mr. Gorman believes that regulated utility companies have lower operating and business risk than the deregulated affiliate companies. Lower operating risk for regulated companies generally is attributable to cost-based price setting, setting rates in a manner that helps to preserve the utilities' financial integrity, utility limited competition, and supportive regulatory oversight available to Canadian regulated utility operations.

**3.4** Please provide any evidence in Mr. Gorman's possession that provides credit ratings associated with the regulated subsidiaries of each of the five Canadian utilities listed in Table 3.

**Response 3.4**

Please refer to Carpenter Attachment 3.1.

**4. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, page 44, lignes 20-21 **Préambule :** « [...] *Standard & Poor's generally finds that Gaz Metro is a low risk gas distribution company [...]* »

**Demandes : 4.1** Please provide a complete copy of the Standard & Poor's document(s) cited on pp. 45-6.

**Response 4.1**

The S&P report cited on pages 45-56 of Mr. Gorman's written evidence was provided as Gaz Métro-7, Document 10.

**4.2** Please provide a reference to any statements by Standard & Poor's (or any other analyst or credit rating agency that Mr. Gorman is aware of) to the effect that Gaz Métro has lower business risk than other gas distribution companies.

**Response 4.2**

Mr. Gorman did not make the assertion in the question. S&P did conclude that Gaz Métro has "Low" business risk. See Mr. Gorman's evidence at 46.

**5. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, page 46, lignes 18-21

**Préambule :** « *Dr Carpenter found that Gaz Metro had uniquely high business risk which would suggest it should be permitted a higher rate of return relative to Canadian utilities and US LDCs. This directly contradicts S&P's finding that Gaz Metro has low business risk* »

**Demandes :** 5.1 Please provide any S&P findings or statements (or those of any other credit rating agency or analyst) in Mr. Gorman's possession that conclude that Gaz Métro has either a) lower or b) similar business risk relative to Canadian utilities or US LDCs.

### **Response 5.1**

Please see page 5 of the S&P report, Gaz Métro-7, Document 10, under Strong Business Risk Profile. There, S&P states:

The Regie de l'énergie (in Quebec) and the National Energy Board regulate GMI's Canadian operations. The regulation for the Quebec distribution assets is similar compared with regulation in other provinces.

Performance-based regulation limits any downside risk to a cost-of-service and rate-of return method. In 2008, the total authorized base ROE was 9.05% (10.37% was achieved), and it is 8.76% for 2009. Although the base rate is fixed, productivity gains allow GMLP to potentially earn up to 375 basis points more than the base rate of return. Similar to other Canadian regulatory jurisdictions, the company is insulated from commodity price risk by directly passing these costs to distribution customers. Quebec regulation also allows for a weather- and wind-normalization deferral account. Rates are calculated on normal weather and wind velocity (30-year average); any variation is deferred through a normalized account and collected from our return [sic] to customers through rate adjustments over a five-year period. Interest-rate risk is also not a ratings concern, because GMLP can defer any variation in interest rates through a normalization account.

Unique to the regulatory environment in Quebec, the distribution operations have formal overearnings sharing mechanism that supports GMLP's ability to generate incentive earnings greater than the regulated base ROE. (Emphasis added).

Also, at page 8 of the same report, S&P rates Gaz Métro's bond rating to be Stable and comparable to the other Canadian utilities.

**5.2** Please provide the basis for Mr. Gorman's assertion at p. 47 ll. 5-6 that S&P recognizes that *"environmental regulations may mitigate Gaz Metro's [competitive] risk with fuel oil and may actually provide gas a competitive advantage relative to fuel oil"*.

**Response 5.2**

Please see S&P report referenced in response to 4.1 above.

**6. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, pages 48-49

**Demandes : 6.1** Please provide the documentary evidence on which Mr. Gorman relies for his characterization of the regulatory mechanisms that apply to Atlanta Gas Light.

**Response 6.1**

See Carpenter Attachment 6.1.

6.2 Does Mr. Gorman believe that AGL has higher business risk than Gaz Métro?

**Response 6.2**

Yes.

**6.3** If so, please provide the analysis on which Mr. Gorman relies to conclude that AGL has higher business risk than Gaz Métro.

**Response 6.3**

See Mr. Gorman's direct evidence at 47-48.

**7. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, page 48

**Demandes : 7.1** Please provide the documentary evidence on which Mr. Gorman relies for his characterization of the regulatory mechanisms that apply to Laclede Gas Group.

**Response 7.1**

See Carpenter Attachment 7.1.

7.2 Does Mr. Gorman believe that Laclede has higher business risk than Gaz Métro?

**Response 7.2**

Yes.

7.3 If so, please provide the analysis on which Mr. Gorman relies to conclude that Laclede has higher business risk than Gaz Métro.

**Response 7.3**

See Mr. Gorman's evidence at 48.

**8. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, pages 48-49

**Demandes : 8.1** Please provide the documentary evidence on which Mr. Gorman relies for his characterization of the regulatory mechanisms that apply to Northwest Natural Gas.

**Response 8.1**

See Carpenter Attachment 8.1.

**8.2** Does Mr. Gorman believe that Northwest Natural has higher business risk than Gaz Métro?

**Response 8.2**

Yes.

**8.3** If so, please provide the analysis on which Mr. Gorman relies to conclude that Northwest Natural has higher business risk than Gaz Métro.

**Response 8.3**

Please see Mr. Gorman's evidence at 48-49.

**9. Références :** (i) ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, page 50, ligne 9; (ii) ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, page 51, ligne 5

**Demandes : 9.1** Please provide copies of any academic studies of which Mr. Gorman is aware that compare the country risk of Canada with that of the US.

**Response 9.1**

Mr. Gorman is not aware of an academic study commenting on the comparison of this country risk.

**9.2** Please provide copies of any practitioner studies of which Mr. Gorman is aware that compare the country risk of Canada with that of the US.

**Response 9.2**

Country risk is included in S&P's bond rating review of Canadian and U.S. Utility Bond Listings.

As noted at pages 50-51 of Mr. Gorman's evidence, U.S. utilities gave greater financial risk but comparable bond rating. The implication from this is that the Canadian utilities have lower operating risk (including country risk) compared to that of U.S. utilities.

**9.3** Please provide the evidence on which Mr. Gorman bases his opinion that country risk is an important consideration in evaluating the business risk of a Canadian utility compared with that of a US utility.

**Response 9.3**

Please see Mr. Gorman's evidence at pages 50-51.

**9.4** Based on his reading of the S&P report quoted with respect to country risk, is it Dr. Gorman's opinion that country risk is higher or lower in Canada relative to the United States? In answering this request, please describe in detail the "economic, financial, regulatory and industry-related risks" that make Canada more (or less) risky than the United States for a gas distribution utility.

**Response 9.4**

Mr. Gorman is not aware of specific S&P findings or conclusions of whether the country risk in Canada is higher or lower than the U.S. country risk.

**10. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, pages 47, lignes 6-10

**Demandes : 10.1** Please confirm that it is Mr. Gorman's opinion that the cost of capital Gaz Métro has applied for should be denied because it would have the effect of raising rates to Gaz Metro's customers.

**Response 10.1**

The question falsely represents Mr. Gorman's written evidence. Mr. Gorman recommends that Gaz Métro's proposed ATWACC methodology, and estimated overall rate of return should be rejected because it is excessive and over-compensates investors for the risk of providing capital to Gaz Métro. The fact that an excessive rate of return will result in an unnecessary increase in prices and increase to Gaz Métro's operating risk is additional reason to find that the proposed ATWACC methodology is detrimental to the best interest of both ratepayers and investors.

**10.2** If that is not confirmed, please explain how the referenced passage in Mr. Gorman's testimony is relevant to the Régie's determination of Gaz Metro's cost of capital?

**Response 10.2**

From a policy perspective, the Régie should thoroughly consider the ramifications of awarding Gaz Métro an excessive overall rate of return. One such negative consequence of awarding an excessive rate of return is that it will erode the competitive position of Gaz Métro, and impair its ability to compete with lower cost alternative energy suppliers. While the determination of a fair and reasonable rate of return should not be based on the relative impact on rates, the need to prevent and award an excessive rate of return and all the negative ramifications that would be produced by such a regulatory action should be considered and understood by the Régie.

**11. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, pages 49, lignes 5-8

**Demande : 11.1** Please provide the evidentiary basis for Mr. Gorman's assertion in the referenced passage.

**Response 11.1**

The basis for this assertion is based on Mr. Gorman's review of regulatory mechanisms for the companies included in the sample groups, relative to the earnings protection provided to Gaz Métro as assessed by Standard & Poor's credit rating reviews of Gaz Métro.

**12. Référence :** ACIG-7, Document 1, *Written evidence of Michael Gorman for IGUA*, pages 49, lignes 11-24

**Demande : 12.1** Please provide Mr. Gorman’s “complete assessment of the affiliated risk exposure of the US gas LDCs [in Dr. Vilbert’s sample] compared to Gaz Metro.” If Dr. Gorman has not prepared such an assessment, please explain why not.

**Response 12.1**

Mr. Gorman has not performed an affiliated risk impact on the bond ratings for the U.S. gas LDCs. The point of Mr. Gorman’s testimony is to describe why Dr. Carpenter’s business risk assessment related to affiliated risk is incomplete, and not fully useful in assessing how these unregulated affiliates impact the operating risk of the U.S. utility companies. As Mr. Gorman concludes in his testimony, Dr. Carpenter’s affiliate risk assessment should not be relied upon in support of Gaz Metro’s proposed ATWACC.

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