

DR. BOOTH UNDERTAKING #2

Régie de l'énergie
DOSSIER: R-3752-2011
DÉPOSÉE EN AUDIENCE Phase 2
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Pièces n°: C-ACIG-0077

To indicate when he started using ranges for his ROE recommendation.

ANSWER

Dr. Booth has always provided a point recommendation such as the 8.10% recommended ROE in this hearing. However, he has always indicated that there is a range in the estimates, for example Dr. Booth has used a beta range such as the 0.45-0.55 range used in this hearing at least as far back as his Hydro One (Dr. Booth Testimony page 58) where data was provided in answer to GMI information request #1 Dr. Booth has never provided a range for the forecast LTC yield on the financial flexibility (flotation cost) addition.

In terms of the market risk premium, Dr Booth provides his own estimates and used 5.0% based on similar material to that provided in his Appendix B in this hearing. In 2009 he received a copy of Dr. Fernandez' survey results on the market risk premium. He initially used this in his Newfoundland Power, Gaz Metro and Terasen Gas testimony in 2009 to include a "margin of error" of 0.25%. This was Dr. Booth's average beta of 0.50 times the 1.0% spread difference between the high and low median market risk premium estimates or 0.50%, weighted equally with Dr. Booth's own estimate. The following passage from Dr. Booth's Terasen Gas evidence (page 61) indicates how this was done.

“Q. YOU PREVIOUSLY MENTIONED A MARGIN OF ERROR, WHAT DOES THIS MEAN?”

A. My recommendation is based on estimates and these always have some measurement error attached to them. As I noted previously the Fernandez article has indicated to me that most Canadian finance professors use 5.0% or 6.0% for the market risk premium. So with a beta of 0.50 this means that in all likelihood another Canadian finance professor might have estimated a fair return 0.50% higher than my estimate. However, when I look at the betas for utilities, either individual companies or the utility sub indexes, it is difficult to see how anyone could estimate a beta for a Canadian utility higher than my .45-0.55 range. Adjusting for the Bell Canada effect we simply haven't seen betas consistently outside of this range for 20 years.

So overall I would indicate that the margin of error in my estimates might be 0.50% which means 7.50-8.0%. Taking the mid point I would recommend a fair ROE of 7.75%. “

Starting with his Line 9 testimony before the NEB in 2010 Dr. Booth incorporated the “margin of error” of 0.25% directly into his market risk premium using a range of 5.0-6.0%.

Dr. Booth started recommending that the ROE adjustment model be extended to include a credit spread adjustment in 2010 at which time he also started recommending a financial crisis premium or spread adjustment of 25-50 basis points (currently 25-40).