BLUME ADJUSTMENT

VILLADSEN WRITTEN RESPONSE

The Régie requests that references supporting the following assertion be provided: "The Blume adjustment procedure is routinely performed by providers of financial data and analysis, such as Bloomberg and Value Line. It is therefore widely relied upon by financial practitioners and accepted by <u>many regulatory agencies</u>"

Dr. Villadsen is aware that the following regulatory agencies rely upon adjusted betas when determining the cost of equity for a utility:

- **Federal Energy Regulatory Commission:** The FERC methodology for estimating the cost of capital for regulated entities requires the use of adjusted betas as reported by *Value Line*. The FERC affirmed the use of adjusted beta in its most recent cost of capital methodology order when it said, "We continue to find reasonable the use of *Value Line* adjusted betas in the CAPM methodology…As we found in Opinion No. 569, there is substantial evidence indicating that investors rely on *Value Line* betas in making investment decisions." (Order 569-A, 171 FERC ¶ 61,154 (2020) at paragraph 75)
- **U.S. Federal Communications Commission:** FCC 16-33, WC Docket No. 10-90, WC Docket No. 14-58, and CC Docket No. 01-92, issued March 30, 2016 para 300 explicitly notes the use of adjusted betas.
- **New York Public Service Commission**: The Commission Staff has an established methodology for estimating the cost of equity. The methodology exclusively relies on adjusted betas as reported by *Value Line*. For example, in the most recently concluded rate case for National Grid, Commission Staff relied upon adjusted *Value Line* betas in its CAPM approaches (NYS DPS 19-G-0309 and 19-G-0310, Staff Finance Panel Testimony, January 30, 2020, p. 65)
- **Regulatory Commission of Alaska:** U-08-157, Order No, 10, February 11, 2010 p. 40 shows the Commission relies on Value Line betas.
- **Oregon Public Service Commission**: Staff Testimony by Matt Muldoon in Docket UE 295, 2015, p. 37 use Value Line betas.
- **Illinois Commerce Commission**: Staff at the ICC use adjusted betas from *Value Line* in their cost of equity estimation. For example, in the recent Nicor Gas rate case, ICC Staff member Phipps says that she uses adjusted betas because "Adjusting the raw beta estimates towards the market mean value of 1.0 results in a linear relationship between the beta estimate and realized return that more closely conforms to CAPM predictions." (Docket No. 21-0098, Phipps Direct Testimony, May 11, 2021, p. 20)

- **Michigan Public Service Commission**: Staff at the MPSC use adjusted *Value Line* betas in their cost of equity analysis. See for example DTE Gas Case No. U-20642, Direct Testimony of Joseph Ufolla, pp. 18-19
- **Alberta Utilities Commission**: In the 2013 Generic Cost of Capital (GCOC) proceeding, the AUC recognized that adjusted betas provide better predictors of equity returns. Paragraph 129 of the 2013 GCOC Decision states: "… the Commission is, nonetheless, mindful of Ms. McShane's conclusion that betas calculated using historical data may be poor predictors of an investor's required or expected return. The Commission also understands that, as one possible solution to this problem, equity market practitioners may use adjusted betas, which, according to some academic research, are better predictors of returns than "raw" betas (i.e., betas calculated using historical data)."