Q. Dr. Cleary Evidence, Page 37, Lines 9-13: In Dr. Cleary's opinion, what steps should Newfoundland Power take to reduce its common equity ratio from 45.0 percent to 40.0 percent? Does Dr. Cleary support the proposal of Dr. Booth to treat this 5.0 percent differential as preferred stock for ratemaking purposes, or does Dr. Cleary have an alternative proposal for this change would be effectuated?

A. Dr. Cleary's analysis was based on the premise that NP would issue additional long-term debt to reduce the common equity ratio. His calculations suggest that a debt issue in the vicinity of $125 million would work; although this could be combined with having NP pay a special "one-time" common share dividend on common shares to accomplish the task, if deemed desirable. Given that NP's borrowing costs are at, or near, an all-time low, this option would provide NP with inexpensive long-term financing.

Dr. Cleary has viewed Dr. Booth's recommendation regarding the use of preferred shares. According to Dr. Booth's calculations the pre-tax cost would be in a similar range to long-term debt at just over 4%; although preferred shares would be slightly more expensive to NP since the dividends are not tax deductible to NP. As noted by Dr. Booth, an issue over $100 million is of reasonable size to be sold in the Canadian preferred share market. While slightly more expensive due to the lack of associated tax shield, this option could be a viable option during a transition period to long-term debt, and it would make the metrics look even stronger than if long-term debt was issued.