Q. Evidence of Ms. McShane Page 3 lines 64-65

(a) Please indicate (with full references and citations) any ROE decisions by a Canadian regulator in the last ten years that has placed any weight on comparable earnings testimony in the manner developed by Ms. McShane for Newfoundland Power.

(b) Please indicate (with full references and citations) any ROE decisions by a Canadian regulator in the last twenty years that has placed any weight on comparable earnings testimony in the manner developed by Ms. McShane for Newfoundland Power without a market to book adjustment.

(c) Please indicate (with full references and citations) any ROE decisions by a Canadian regulator in the last ten years that has placed any weight on discounted cash flow estimates in any manner, particularly as implemented by Ms. McShane for Newfoundland Power.

(d) Please indicate (with full references and citations) any ROE decisions by a Canadian regulator in the last ten years that has placed any weight on direct evidence of the fair ROE derived from US utilities or US stock market performance.

A. (a) Ms. McShane is not aware of any decisions in the past 10 years which have given weight to the comparable earnings test as applied by Ms. McShane. In arriving at its cost of capital decision for TGI and TGVI in March 2006, the British Columbia Utilities Commission stated that it did not believe comparable earnings had outlived its usefulness, and that it may yet play a role in future ROE hearings. The BCUC did conclude in that decision that there was insufficient evidence before it regarding whether or not a market/book ratio adjustment was merited and, if so, how it might be accomplished. As indicated at pages F-6 to F-9 of her testimony in this proceeding, Ms. McShane explains why an adjustment is not warranted.

(b) In RH-2-92 (2/93) for TransCanada PipeLines, the National Energy Board stated,

> "Both the comparable earnings and equity risk premium techniques provided the Board with useful information in its determination of the appropriate rate of return to be allowed on TransCanada's deemed common equity component. However, the Board remains of the view that the results of the risk premium method should be given more weight than those of the comparable earnings method. The NEB decision did not discuss the need for a market to book adjustment.

In E95070 (6/95) for the City of Edmonton, the Alberta Energy and Utilities Board stated,

> "In arriving at a rate of return on common equity, the Board considers that, for the purposes of this Decision, all three tests of measuring common equity return are relevant. The Board does not agree with the opinion of the witness for the ERWCG, Mr. Kahal, that the comparable earnings test is of little help or relevance to these hearings because it does not attempt to measure the market cost of equity for the companies in the comparison sample. Rather, the Board considers that there is still some merit in the comparable earnings test to the extent that regulation is considered a surrogate for competition and the comparable earnings test attempts to measure the achieved accounting rates of return on common equity of enterprises of similar risk. The Board does, however, recognize that there may well be distortion in the market to book ratios caused by the effects of inflation on retained earnings of companies, notwithstanding their similarity in risk. Similarly, the comparable earnings test may be sensitive to the selection of the business cycle under study." The AEUB did not mention the need for a market to book adjustment.

(c) The BCUC gave weight to the DCF method as applied by Ms. McShane in its March 2006 decision. At page 55 of the decision, the BCUC stated "The Commission Panel is more persuaded by Ms. McShane's evidence which compares Value Line and I/B/E/S forecasts and finds no upward bias in the latter. Accordingly, the Commission Panel will give weight to Ms. McShane's first DCF Test, which yielded an indicated return of 8.8 percent."

(d) The NEB gave weight to evidence derived from U.S. markets and to U.S. utilities specifically in its March 2009 RH-1- 2008 decision for TransQuébec and Maritimes Pipeline. Relevant citations from that decision include:

> "In the Board's view, global financial markets have evolved significantly since 1994. Canada has witnessed increased flows of capital and implemented tax policy changes that facilitate these flows. As a result, the Board is of the view that Canadian firms are increasingly competing for capital on a global basis. The Board notes that Canada has been diversifying its business partners such that there is currently proportionally less Canadian foreign direct investment in the United States than there was in the 1990's. Nonetheless, the evidence is also clear that the United States is the single most important recipient of Canadian investments." (pages 66-67)

> "The Board is satisfied that the evidence establishes that TQM and U.S. LDCs are sufficiently similar in risk so as to make comparisons meaningful." (page 68)

> "Nonetheless, the Board found that litigated U.S. returns were useful as a check against the results from the analyses which relied upon market returns." (page 69)

> "In light of the Board's views expressed above on the integration of U.S. and Canadian financial markets, the problems with comparisons to either Canadian negotiated or litigated returns, and the Board's view that risk differences between Canada and the U.S. can be understood and accounted for, the Board is of the view that U.S. comparisons are very informative for determining a fair return for TQM for 2007 and 2008." (p. 71)

The BCUC gave weight to evidence derived from U.S. utilities inasmuch as it gave weight to the DCF test applied to a sample of U.S. utilities as indicated in c) above. The BCUC also gave weight to U.S. market returns in determining the market equity risk premium.

> "In the Commission Panel's view a MRP of 5.8 percent is appropriate, given the Canadian experienced premiums since the Second World War, adjusted upwards in part to recognize both the fact that bond returns will most likely decrease in future years, and in part to recognize U.S. returns." (page 53)

In its April 2002 Decision D-2002-95, for Hydro Québec Transmission, the Régie de L'Énergie gave 40% weight to U.S. returns in its estimation of the equity market risk premium.

> "Enfin, concernant la question spécifique du pourcentage à accorder entre les etudes canadiennes et américaines retenue par la Régie dans sa décision D-99-150 rendue le 20 août 1999, en accordant une pondération de 40 % aux données d'études américaines, la Régie constate que dans le présent dossier, aucun élément nouveau n'a été présenté en preuve à ce sujet. La Régie considère opportun d'inclure les données américaines dans son estimation de la prime de risque du marché. Pour ces motifs susmentionnés, la Régie décide de maintenir la pondération qui a été édictée par cette dernière décision.