Q. Vander Weide Evidence – Does Dr. Vander Weide agree that a utility's risk of cost disallowances is a risk to an equity investor in a regulated utility? If so, how? If not, why not?

A. Yes. Dr. Vander Weide defines equity risk as the risk that the equity investor will earn a return on equity that is less than the equity investor's required return on equity. Cost disallowances increase risk to an equity investor because cost disallowances increase the risk or probability that equity investors will earn a return on equity that is less than their required return on equity. However, Dr. Vander Weide also recognizes that the risk to the equity investor is not the same as the risk to debt investors. Debt investors are only concerned with the risk that a utility's ROE, and hence earnings, will be insufficient to cover the interest payments on the utility's debt. Equity investors are concerned with the risk that the utility's actual ROE will be less than the equity investor's required ROE.