Q. At p. 21, Mr. McDonald states that, "If the common equity ratio were lowered, credit returns could weaken." Dr. Booth's report, at p. 80, recommends that 5% in common equity be replaced with preferred shares. Dr. Booth makes the following statement at line 15: "However, unlike bonds these [i.e. preferreds] are similar to equity and paid out of after tax income so they therefore support the credit rating, as they do not add fixed interest." Does Mr. McDonald agree with this statement? Why or why not?

A. Mr. MacDonald does not agree with the statement. Mr. MacDonald believes that preferred shares can have characteristics of both debt and equity. As noted by Dr. Booth preferred shares with a retraction feature where the investor can retract or demand payment sell on yields relative to mid-term Canada bonds (pg. 80, lines 13-15). Mr. MacDonald cannot confirm that these preferred shares are similar to equity as Mr. MacDonald agrees with Dr. Booth that they trade similarly to debt (based on yield).

Mr. MacDonald confirms that dividends are paid out of after tax income and interest is paid out of pre-tax income.

Mr. MacDonald confirms that by substituting 5% common shares for 5% preferred shares this will not add fixed interest.