

Q. Opinion on Capital Structure and Return on Equity
Kathleen McShane – Volume 3

Do you believe that changes in a fair return on equity between test years can be estimated accurately using a formula, or is a fair return on equity determination simply too complex to be applied using a formula approach? Please explain your response.

A. In Ms. McShane's opinion, the cost of equity is complex, as multiple factors determine the returns that equity investors require at any given time. However, as noted in response to PUB-NP-078, a formula, under market conditions where interest rates represent normal levels, should be able to broadly account for secular and cyclical changes in the cost of equity.