CHATHAM-KENT HYDRO
A Chatham-Kent Energy Company

Middlesex Power Distribution Corporation

April 17, 2009

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
PO Box 2319
2300 Yonge St, 27th Floor
Toronto ON M4P 1E4

Dear Ms. Walli:

Re: The Cost of Capital in Current Economic and Financial Market Conditions
Board File No. EB-2009-0084

Chatham-Kent Hydro and Middlesex Power Distribution Corporation ("CK-MP)" are pleased to be given the opportunity to provide additional comments on the Ontario Energy Board's ("Board") consultative process, The Cost of Capital in Current Economic and Financial Market Conditions, Board File No. EB-2009-0084**.** Please accept CK-MP's response to questions 2, 3, and 5 followed with general comments as submission to this consultative process.

2. In the context of the current economic and financial conditions, are the values produced by the Board's Cost of Capital methodology and the relationships between them reasonable? Why, or why not?

   CK-MP believes that the decreasing spread between Long-Term Debt and ROE is directionally inconsistent with the accessibility of funds under the current economic conditions. As Debt becomes more difficult to access or becomes more costly under the current economy the alternative for companies to access funds fundamentally becomes more costly to access.

3. What adjustments, if any, should be made to the Cost of Capital parameter values to compensate or correct for the current economic and financial conditions?

   CK-MP only comments to the result of the formula and not to the formula itself (see NEB decision for formula or Cost of Capital parameter adjustment details). For the fair return standard to be met there is a required spread that should be maintained between Long-Term Debt and ROE. Historically, this spread has averaged 250 basis points.

5. Are there other key issues that should be considered if the Board were to adjust any or all of the Cost of Capital parameter values produced by the application of its established formulaic methodology?

CK-MP believes that a change to the formula may be necessary if the resulting ROE calculation results in a spread between Long-Term Debt and ROE that is unreasonable or does not meet the fair return standard. All things considered the spread used in 2001 – 263 basis points, 2008 – 247 basis points. The 2009, 39 basis points spread creates a fundamental disconnect in the 2009 fair return standard. See Table 1.

Table 1

	2001	2008	2009 current	2009 proposed
ROE	9.88	8.57	8.01	10.12
L-TD	7.25	6.10	7.62	7.62
Spread	**2.63**	**2.47**	**0.39**	**2.50**

General Comments:

I. <u>ROE Spread</u>

In reviewing the 2001 rates approved by the Board the ROE used in the approval process was 9.88 and the Long-Term Debt was 7.25. The resulting spread or ‘risk premium’ was 263 basis points. The spread in the 2008 rate approval process was 247 basis points. Whether these spreads or ‘risk premiums’ are reasonable may be subject to debate, it remains that they were calculated using a similar formulaic approach currently used. As well, it is arguable that the 263 and 247 basis point spread between Long-Term Debt and ROE meets the fair return standard that equity investors require due to their different risk profile. Following this methodology it would be reasonable to increase the spread between Long-Term Debt and ROE from the current 39 basis points as this, historically and under current economic conditions, does not meet the fair return standard. Using an average historical spread of 250 basis points between Long-Term Debt and ROE would more accurately reflect both the different risk profiles of investors as well as address more accurately the current economic conditions.

II. <u>National Energy Board (“NEB”) Decision</u>

In the recent decision by the NEB with respect to the approach used in the calculation of cost of capital the NEB changed from their traditional formula ROE (in place since 1995) to a weighted average cost of capital approach. This decision, for the most part, was in response to the unfair return generated using the traditional formulaic approach. The new weighted average cost of capital approach resulted in the calculated ROE increasing by 110 basis points from the traditional formulaic approach. This new approach more fairly represents the different risk profiles for investors and their associated risk profiles. The NEB’s decision goes to the fundamental notion that there should be a reasonable spread between Long-Term Debt and ROE to meet the fair return standard.

CK-MP thanks the Board again for the opportunity to participate in this consultative process for "The Cost of Capital in Current Economic and Financial Market Conditions".

If you have any questions or concerns, please do not hesitate to contact Garry Symons.

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