PUBLIC INTEREST ADVOCACY CENTRE
LE CENTRE POUR LA DÉFENSE DE L'INTÉRÊT PUBLIC

August 2, 2024 **VIA E-MAIL**

Ms. Nancy Marconi
Registrar (registrar@oeb.ca)
Ontario Energy Board
Toronto, ON

Dear Ms. Marconi:

Re: EB-2024-0063 Generic Cost of Capital Proceeding
Interrogatories of the Vulnerable Energy Consumers Coalition (VECC)
to NEXUS Economics (NEXUS) Exhibit M3 – Electricity Distributors Association (EDA)

Please find attached the revised interrogatories of VECC in the above-noted proceeding. We have also directed a copy of the same to the Applicant.

Yours truly,

Mark C. Garner Digitally signed by Mark C. Garner
Date: 2024.08.02 16:50:04 -04'00'

Mark Garner
Consultants for VECC/PIAC

Email copy:
Ted Wigdor, VP EDA
twigdor@eda-on.ca
Brittany Ashby, Senior Regulatory Advisor, EDA
bashby@eda-on.ca

REQUESTOR NAME	**VECC**
TO:	**EXHIBIT M3: EDA / NEXUS ECONOMICS (NEXUS)**
DATE:	**August 2, 2024**
CASE NO:	**EB-2024-0063**
APPLICATION NAME	**GENERIC COST OF CAPITAL PROCEEDING**

1.0 Reference: M3: NEXUS Report, page 2

Preamble: The Report states:
"*Other issues that the OEB identified are not addressed in this report, either because we were instructed that they were not relevant to the EDA membership or we had no significant criticisms to the LEI conclusions. However, the absence of an opinion on any issue should not be construed as support of the LEI analysis about that issue*."

1.1 With respect to those issues that NEXUS did not address (Table 2), please identify those where NEXUS "*had no significant criticisms to the LEI conclusions"*.

2.0 Reference: M3: NEXUS Report, pages 3-5, 22 and

Preamble: The Report states (page 4):
"*The coloured lines and dots in Figure 1 represent the comparator states and provinces selected by Nexus Economics and described in Chapter III (Benchmarking). The grey "spider web" in Figure 1 represents the other US states*."
And
"*We also added "re-levered" Alberta and British Columbia returns since these jurisdictions use a 55 percent Debt capital structure (more equity than is currently the case in Ontario*)."

The Report also states (page 84):
"*British Columbia and Alberta have Deemed Debt Ratios of 55 percent*."

2.1 With respect to Figure 1 and Figure 5, does the BCUC approve a common equity thickness and ROE which is applicable to all BCUC regulated utilities?

2.1.1 If not, what is the authorized value (or range of authorized values) for equity thickness and ROE for electric utilities (and more specifically electric utilities with minimal generation assets)?

2.1.2 If not, how was the single point value included in Figure 1 for BC determined?

2.1.3 Please provide the calculation supporting the British Columbia 2024 Re-levered value shown.

2.2 With respect to Figure 1 and Figure 5, does the AUC approve a common equity thickness and ROE which is applicable to all AUC regulated utilities?

2.2.1 If not what is the authorized value (or range of authorized values) for equity thickness and ROE for electricity distributors?

2.2.2 If not, how was the single point value included in Figure 1 for Alberta determined?

2.2.3 Please provide the calculation supporting the Alberta 2024 Re-levered value shown.

2.3 Similarly, with respect to Figure 1 and Figure 5, do California, Massachusetts and New York each approve a common equity thickness and ROE which is applicable to all regulated utilities?

2.3.1 If not, how was the single point value included in Figure 5 for each state determined?

3.0 Reference: M3: NEXUS Report, pages 5 and 36-37

Preamble: The Report states (page 5):
"*As a result of our independent analysis, to meet the FRS, we recommend a fair return on equity be established at 11.08 percent. This result includes 50 basis points for transaction costs associated with acquiring the equity, which is a continuation of existing OEB policy*."

3.1 Did NEXUS undertake any analysis to determine if 50 basis points was a reasonable/appropriate allowance to include for transaction costs associated with Ontario's electricity distributors acquiring equity?

3.1.1 If yes, please provide these details.

4.0 Reference: M3: NEXUS Report, page 6

Preamble: The Report states:
"*LEI proposes that Transaction Costs be excluded from the ROE and instead be expensed, thereby disregarding IAS and IFRS accounting rules*."

4.1 Is it necessary for the OEB to follow IAS and IFRS accounting rules for purposes of setting regulated utilities' rates?

5.0 Reference: M3: NEXUS Report, pages 8 and 24

Preamble: The Report states (page 8):
"*Changes in the electric utility market influence the level of risk to which the distributors are exposed, thus impacting the ROE which the utility is required to receive. Distributors in Ontario are facing significant risks associated with the energy transition and other events. As a result of these risk factors, capital spending is expected to increase markedly,*

triggered by significant load growth, grid hardening, and cyber-security investments. These risk factors can result in a required return on equity greater than those of its would-be peers." (emphasis added)

The Report also states (page 24):
"*Various risk factors exist for electric distributors. These risk factors change over time. In some cases, the industry could be relatively low-risk. Conversely, at other times, the level 10 of risk could increase due to exogenous factors that are uncontrollable by the utility. As a result of the changes in the level of risk, the ROE of the utility should also be adjusted to reflect these factors*." (emphasis added)

5.1 What are the "other events" that NEXUS is referring to on page 8?

5.2 Is it NEXUS contention that the Ontario electricity distributors' peers (i.e. electricity distributors in other jurisdictions) are not facing similar risk factors?

5.2.1 If yes, please explain why this is the case?

5.3 Does NEXUS agree that energy transition and these other events represent business risks?

5.3.1 If not, why not?

5.4 Is it NEXUS view that changes in business risk should be reflected in changes to a utility's ROE as opposed to changes in its capital structure (i.e., equity thickness)?

6.0 Reference: M3: NEXUS Report, page 8 and 20-21

Preamble: The Report states:
"*While there are several risks facing Ontario utilities, there can be none more fundamental than the imminent energy transition, sometimes also referred to as "electrification." Currently, the electric power industry is facing an energy transition that has not been experienced in the past half-century. Ontario's embrace of decarbonization is triggering electrification and growth in significant demand*."

6.1 Please identify those recent Ontario government policy and/or legislative changes that demonstrate Ontario is embracing decarbonization.

6.2 How would NEXUS characterize Ontario's embracing of decarbonization relative to that of the five comparable/peer regulatory environments identified on pages 20-21?

7.0 Reference: M3: NEXUS Report, pages 10 and 27

Preamble: The Report states (page 10):
"*In both the Reference Scenario and the Net Zero Case the level of distribution investments is anticipated to increase significantly. Historically, distributors have been required to make annual distribution*

investments of $2.63B. Annual distribution investments for the Reference and Net Zero cases are projected to be an average of $3.81-4.46B between 2024 and 2050. The net zero scenario increases annual capital by 70 percent compared to historical spending. This last point is crucial, because the investment required by the energy transition is not far off in the future: substantial investment is required in under 5 years." (emphasis added)

7.1 Under each of the two cases, what is the average annual distribution investment required over the period: i) 2024 to 2030 and ii) 2031-2035?

7.2 Please provide a copy of the referenced EDA Report.

8.0 Reference: M3: NEXUS Report, pages 11 and 16

Preamble: The Report states (page 11):
"*Evidence contradicting LEI's claim that Ontario's regulatory mechanisms reduce risk is its own Figure 19, which illustrates that, on average, a group of 54 Ontario distributors are not earning their deemed return. The systematic underearning does not support the claim that the regulatory environment in Ontario is as safe as LEI claims*."
And
"*The FRS expressly refers to an opportunity cost of capital concept, meaning it is prospective rather than retrospective*." (page 16)

8.1 Is it NEXUS's contention that the underearning by Ontario's electricity distributors is solely (or even primarily) due to the regulatory environment in Ontario?

8.2 Please reconcile NEXUS' using of actual/retrospective data to support its claim that the Ontario's regulatory environment is not supportive with the acknowledgement that the FRS expressly refers to an opportunity cost of capital concept, meaning it is prospective rather than retrospective.

9.0 Reference: M3: NEXUS Report, page 18

Preamble: The Report states:
"*Only peers operating in the Canadian / U.S. financial markets should be included in the Board's comparable analysis. Firms operating in other financial markets, including the UK and Australia, operate under different legal, institutional, and macroeconomic circumstances which could influence utility ROEs*."

9.1 Is it NEXUS's contention that firms/utilities in the US operate under the same legal and institutional circumstances as those operating in Canada? If yes, why?

9.2 Why are U.S. comparators inherently better than those of the UK and Australia whose legal system and institutions may actually be more closely aligned with Canada (for example by a shared commonwealth of legal, political and financial institutional forms).

10.0 Reference: M3: NEXUS Report, page 19

Preamble: The Report states:
"Fortis BC has been included because it has limited electric generation capacity."

10.1 Electric generating capacity represents what proportion of FortisBC's rate base?

11.0 Reference: M3: NEXUS Report, page 22

Preamble: The Report states:
"*Deemed Debt-to-Capital Ratio in Ontario is 60.0 percent. The average Authorized Debt-to-Capital Ratio for all of the comparables is lower. California is 48.8 percent; New York is 52.0 percent; Massachusetts is 49.7 percent; British Columbia is 55 percent; and Alberta is 55 percent. (Sources are S&P SNL data for US comparables and various Decisions for British Columbia and Alberta*.)"

11.1 Please confirm that, per BCUC Order G-236-23 (page 151), the deemed equity component for FBC is 41%.

12.0 Reference: M3: NEXUS Report, page 25
M1: LEI Report, pages 54-55

Preamble: The Report states:
"*LEI has identified business and financial risks in its report. However, given the changes in industry structure occurring due to decarbonization and electrification efforts, Nexus Economics has also identified a category of risk that LEI ignores: strategic risk. Strategic risk is the risk that distributors are subjected to as they face increasing uncertainty regarding the direction of the industry and the significant investments that they will be required to make despite the uncertain future. Therefore, Nexus Economics considers that LEI fails to recognize the magnitude of the changes the distributors likely will encounter now and in the coming years*."

12.1 Please clarify whether it is NEXUS' contention that LEI has: i) missed a risk category (i.e. "strategic risk") or ii) failed to recognize the magnitude for risk associated with energy transition.

12.2 If it is NEXUS's view that LEI has missed "strategic risk" as a risk category, please explain how NEXUS's strategic risk category reflects risks that re not captured under LEIs energy transition risk and policy risk categories.

12.3 Why would "electrification" or "strategic risk" which describes a process of increasing reliance on electricity (production and distribution) and hence greater overall growth than otherwise would be the case represent be a risk requiring greater shareholder compensation than in the past? Can NEXUS provide examples of companies in other market sectors going through high growth demand periods which have be seen in the market as more risky investments than when demand for their product was lower?

13.0 Reference: M3: NEXUS Report, page 33
M1: LEI Report, page 129, Figure 47

Preamble: The Report states:
"*Nexus Economics cannot conclude that the regulatory environment offered in Ontario is significantly safer than its peers and, therefore, should be provided with a lower ROE*."

13.1 Does NEXUS consider the regulatory environment offered in Ontario to less safe than that offered by its peers?

13.1.1 If yes, please reconcile this view with Figure 47 in the LEI Expert Evidence which indicates that Ontario is one of the jurisdictions that S&P rates as being "Most Credit Supportive" while Massachusetts and New York have less favourable ratings.

14.0 Reference: M3: NEXUS Report, pages 34-35

Preamble: The Report states:
"Procuring debt or equity capital is not itself without cost. Some of the costs are direct, such as reimbursements or payments to lenders, underwriters, investment banks, or rating agencies. Other costs are indirect, as in the case of an equity issue that would dilute the value of existing shares." (page 34)
And
"*Because the transaction costs for debt and for equity are incurred only when the utility actually obtains new debt or equity, if the transaction costs for debt occurs between Board reviews, this legitimate, quantifiable, and known expense would not be recovered. This is contrary to the Fair Return Standard because it does not provide an opportunity for the utility to earn its authorized return*." (page 35)

14.1 Please provide NEXUS's understanding as to the main sources of debt financing used by Ontario's electricity distributors.

14.1.1 For each of these sources, please indicate what types of transaction costs would be incurred and whether they would be one-time costs.

14.2 Would it also not be the case that if transaction costs of debt were forecasted as an expense for the year a distributor was rebasing and no further borrowing occurred prior the next rebasing then the inclusion these costs in the PBR formula's base year could lead to an over-recovery of the allowed ROE.

15.0 Reference: M3: NEXUS Report, page 36

Preamble: The Report states:
"Like debt transaction costs, equity transaction costs are incurred in acquisition by the utility of equity capital from the marketplace. These costs are associated with any type of equity acquisition. If they are expensed as operating costs but not actually recoverable, the result will

be underperformance of the utility with regard to its potential 1return. Expensing these costs, absent some sort of adder to customer bills, means that the expenses will not be recovered."

15.1 Please provide NEXUS's understanding as to the main sources of equity financing used by Ontario's electricity distributors.

15.1.1 For each of these sources, please indicate what types of transaction costs would be incurred and whether they would be one-time costs.

16.0 Reference: M3: NEXUS Report, page 42

Preamble: The Report states:
"*Ontario electricity distributors must raise capital funds from somewhere and it is important to understand how scarce funds are allocated in the market*."

16.1 How many of Ontario electricity distributors have raised debt in the US capital markets?

16.2 How many of Ontario electricity distributors have raised equity capital in the US capital markets?

16.3 In NEXUS's view would it be reasonable to expect that most Ontario electricity distributors would be able to access the both debt and equity capital in the US capital markets?

17.0 Reference: M3: NEXUS Report, page 47

Preamble: The Report states:
"*Second, regarding LEI's DCF results, we left them unchanged. We did not make a leverage adjustment because publicly traded US electric utilities generally have (book) Debt-to-Equity ratios around 60:40 which is the same as the Deemed Debt Ratio, so there was no need to do so*."
And
"*Third, regarding LEI's risk premium method, we input a forecasted US debt rate and a contemporary Moody's Baa bond rate into LEI's forecasting equation. We unlevered and relevered the results using the formula that is described later in this report to make the financial risk associated with the DCF and risk premium results more like that of the Ontario electric service providers. US regulated electric service providers generally have authorized Debt-to-Equity ratios of around 50:50. The Ontario Deemed Debt Ratio is 60:40, which implies more equity risk, so we make the adjustment*."

17.1 With respect to the first quote, is there a difference in the debt-to-equity ratios as between those publicly traded US electric utilities that are integrated (i.e., include generation as well as transmission and distribution assets) as compare to those that whose asset base is primarily/wholly electricity transmission and distribution assets?

17.2 With respect to the second quote, is there a difference in the authorized debt-to-equity ratios as between those US regulated electric service providers that are integrated (i.e., include generation as well as transmission and distribution assets) as compare to those that whose asset base is primarily/wholly transmission and distribution assets?

18.0 Reference: M3: NEXUS Report, pages 45 and 49

Preamble: The Report states:
"*The above analysis of the Canadian and US economies is indicative of a single capital market*." (page 45)
And
"*It is the third step that contains the error. Using the 2025 forecasted Canadian rate of 3.19 percent (for example, as of 6/25/2024, the Canadian yield is 3.295 percent versus the US rate of 4.39 percent) in place of the US rate accounts for the difference. It is incorrect to swap out a US dollar-based rate for a Canadian dollar-based rate when the original data series still exists*." (page 49)

18.1 If the Canadian and US economies are indicative of a single capital market, why is there a significant difference between the 2025 forecast Canadian rate of 3.19% and the 2025 forecast US rate of 4.39%?

18.2 How are exchange rates and exchange rate risk considered/imputed into NEXUS theory that Canada and the U.S. share a unified market?

19.0 Reference: M3: NEXUS Report, page 50

Preamble: The Report states:
"*In its Figure 41, LEI attempts to compute a CAPM ROE using Canadian data but returns a result that LEI recognizes as manifestly useless. LEI concludes that "the CAPM ROE based on Canadian market data (5.14 percent) does not reflect investors' expected equity returns." We concur—and, in fact, this underscores Nexus' view on the single North American capital market as discussed earlier*."

19.1 Please explain how LEI rejection of the CAPM results based on Canadian data "underscores Nexus' view of a single North American capital market".

20.0 Reference: M3: NEXUS Report, pages 4 and 57

Preamble: The Report states:
"*The ROEs set by the OEB and proposed by LEI are nowhere near the return available from the application of invested capital to other enterprises of like risk*." (page 4)
And
"*In an interest rate environment where US 30-year Treasuries are over 4.0 percent and Moody's Baa bonds are about 5.80 percent, Ontario electric service providers simply are not in the game at the LEI proposed base rate of return of 8.95 percent, or, indeed, at the current rate of return of 9.21 percent*." (page 57)

20.1 Please provide any evidence NEXUS is aware of that indicates Ontario's electricity distributors are not "in the game", i.e., have been unable to access capital at competitive rates when seeking to do so.

21.0 Reference: M3: NEXUS Report, pages 59-61

Preamble: The Report states:
"*We kept only those firms that traded on North American exchanges (NYSE, NASDAQ, 9 TSX, and OTC). We then examined each of the surviving candidates for special issues that made them inappropriate for comparison. We rejected those that (1) had no operations; (2) no longer existed; (3) were REITs rather than operating companies; (4) had no distribution or transmission (were IPPs, engineering companies, developers, or marketers) (5) only renewables or biogas (too speculative); (6) had considerable negatives in the historical data such as no revenues or no history of positive earnings (too speculative*)."

21.1 Please explain why the requirements that: i) the company be paying dividends (so as to provide a positive dividend yield for input to the DCF model) and ii) the company have an investment grade credit rate were not included as screening criteria.

21.2 Please confirm that the screening criteria used will not "screen out" companies where generation is a significant portion of their asset base but not 100%.

21.3 Is NEXUS able to identify those companies its list where a significant portion (e.g., greater than 70%) of the assets and/or revenues come from generation as opposed to transmission and distribution?

21.3.1 If so, please provide a revised list with these companies removed.

21.3.2 If so, how would using this revise list impact NEXUS's cost of equity calculations using: i) the CAPM (per pages 62-69) and ii) the DCF approach (per pages 70-72)?

22.0 Reference: M3: NEXUS Report, pages 62-64

22.1 Please confirm that the earnings growth rate used the DCF Model for purposes of determining the MRP was 11.49%. If not confirmed, what was the growth rate used?

22.2 Please clarify whether NEXUS used a single stage or multi-stage DCF model to estimate the MRP value.

22.2.1 If a single-stage DCF model was used, please provide NEXUS' rationale for adopting this approach.

22.2.2 If a two or three-stage DCF model was used please indicate the length of time assumed for each stage and the basis for the growth rates used in each stage.

23.0 Reference: M3: NEXUS Report, page 67 (Table 8)

23.1 Table 8 shows the correlation of betas from different sources. Please explain exactly what beta values are being used for purposes of Table 8.

24.0 Reference: M3: NEXUS Report, pages 62 (Footnote #80) and 68

Preamble: The Report states:
"*Applying the CAPM using a forward-looking MRP and interest rates results in an ROE of 10.19 percent excluding the transactions cost recovery of 50 basis points*."

24.1 Please provide the values for each of the parameters of the CAPM formula (per page 62) that result in an ROE of 10.19%.

24.2 Is the 10.19% meant to reflect an appropriate ROE for 2024 or 2025?

25.0 Reference: M3: NEXUS Report, pages 69-72

Preamble: The Report states:
"*As noted earlier, using dividends per share as the Expected Cash to Investors, and price per share as the value metric (in a well-functioning capital market prices equilibrate to value), the Gordon model becomes:*
$k_e = d_0(1+g)/P + g$" (page 69)
And
"*For the dividend yield, we use contemporary yields (i.e., May 2024, when the dataset was downloaded from CapIQ*)" (page 69)
And
"*Since there is considerable dispersion in outlooks for earnings growth, we also filter the growth rates to only use those that are within standard deviations of the overall average (95 percent confidence*)." (page 71)
And
"*Applying our DCF analysis to the data provided by Yahoo, Zacks, CapIQ, and Stock Analysis produces a weighted average DCF cost of equity result of 10.92 percent*." (page 71)
And
"*The lower- and upper- 95 percent confidence interval on this average also found on line 1 of Table 9 is 9.92 percent to 11.93 percent, which excluding transactions costs*." (page 72)

25.1 For purposes of calculating the DCF ROEs for each company did NEXUS use a multi-stage DCF model or was a single stage DCF model used?

25.1.1 If a single-stage DCF model was used, please provide NEXUS' rationale for adopting this approach.

25.1.2 If a two or three-stage DCF model was used please indicate the length of time assumed for each stage and the basis for the growth rates used in each stage.

25.2 With respect to the second reference, please explain more fully: i) how the Dividend Yield value for each company was determined (i.e., was it based

current dividend rates or average dividends over the past year – recognizing that dividend rates change) and ii) how the stock price used in the denominator was determined (e.g., over what period was it averaged and why this period was selected))?

25.3 With respect to the third and fourth references, please provide a list of the companies actually used for the DCF analysis, the dividend yield for each, the growth rate used for each and the resulting DCF ROE for each, and the weighting applied to each company's results – leading to the 10.92%.

25.3.1 Please also explain how the growth rate to be used for each company was determined (e.g., was it a simple average of the growth rates from available sources?).

25.4 With respect to the fourth reference, please explain how the weighting for each company was determined and why it is appropriate to weight the results accordingly as opposed to using a simple average.

25.5 With respect to the fifth (last) reference, was the data used to determine the confidence range the DCF ROE results for each of the individual companies.

26.0 Reference: M3: NEXU Report, page 69
M2: Concentric Report, page 58

Preamble: The NEXUS Report sets out the formula for calculating the DCF ROE as:

$$k_e=d_0(1+g)/P+g$$

In contrast, instead of $k_e=d_0(1+g)/P$, the Concentric Report uses the following as the dividend yield component in the formula:

$$Y = D_0(1+0.5g)/P_0$$

Concentric explains the basis for its formula as follows:

"*One half year's growth rate is applied to the annual dividend rate to account for increases in quarterly dividends at different times throughout the year. It is reasonable to assume that dividend increases will be evenly distributed over calendar quarters. This adjustment ensures that the expected dividend yield is, on average, representative of the coming twelve-month period and does not overstate the aggregated dividends to be paid during that time*."

26.1 Please comment on the two approaches to determining the dividend yield and why the approach used by NEXUS is more appropriate.

27.0 Reference: M3: NEXUS Report, page 74 (Table 9)

27.1 Table 9 provides DCF results for each of the four sources used for the growth rate values. Is part of the reason for the differences in the results (across the four sources) due to that fact that each of the four ROE estimates only used those companies for which the associated source provided a growth estimate?

27.1.1 What other reasons are there (if any) for the differences in the results?

28.0 Reference: M3: NEXUS Report, pages 72-73

Preamble: The Report states:
"*In our analysis, we examine authorized ROEs as a function of interest rates. We used the S&P's SNL Financial data file of US authorized returns on equity*"
And
"*Using a rate of 4.06 percent (2025 forecast for 30-year US Treasury bonds) and Moody's Baa yield of 5.790 percent produces an unlevered ROE of 7.863 percent, which we then relever to the Deemed 60:40 Debt-to-Equity ratio and a tax rate of 26.5 percent to produce an ROE of 11.59 percent, as reported in Table 2. We then remove 50 basis points (for transactions costs) from the risk premium result to produce 11.09 percent*." (page 73)

28.1 What was the time period from which the authorized ROEs were based?

28.2 Did the data used include more than one authorized ROE for each of the companies?

28.2.1 If yes, for any of these companies, did the authorized debt ratio change over the time frame and, if it did, how was this factored into the relevering?

28.3 Please clarify the basis of the 5.79% for the Moody's Baa yield (e.g., is it the current yield or a forecast yield for 2025?).

28.4 If the Moody's Baa yield represents a "current" yield why is it appropriate to use a 2025 forecast for 30-year US Treasury bonds?

28.5 Please explain how the debt-to-equity ratio associated with the unlevered ROE of 7.863% was determined (e.g., is it an average of the debt-to-equity ratios associated with each of the authorized ROE values used?).

28.6 Please re-estimate the equation for Unlevered Authorized ROE using 30-year GOC government bond yields along with the Moody's Baa yields.

28.6.1 Using the resulting equation, please provide an estimate of the current ROE.

29.0 Reference: M3: NEXUS Report, page 76

Preamble: The Report states:
"*Table 2 adjusts all methods and outputs to a 60:40 ratio and also to a tax rate of 26.5 percent (versus US 21 percent*)."

29.1 Should table reference in the quoted part of the Report be Table 9 as opposed to Table 2?

29.2 In Table 9, for which methods was it necessary to adjust the outputs to a 60:40 ratio and a tax rate of 26.5%?

30.0 Reference: M3: NEXUS Report, pages 80-83

Preamble: The Report states:
"*Between the years 2015 and 2022 a sample of Ontario distributors on average did not earn their authorized returns. If a distributor is not earning a return established at the FRS it is operating at an economic loss. These distributors, on average, have operated at an economic loss during each of these years. We conclude that the perspectives of equity investors are not represented by the current Board regulatory mechanisms. We therefore recommend a more frequent (every 3 year) full review of the cost of equity parameters to ensure that investor perspectives are being taken into account*." (page 80 – emphasis added)
And
"*As we noted above, Ontario distributors have on average failed to attain their authorized return on equity in any of the 8 years between 2015 and 2022. Based on LEI's own analysis (as shown in its Figure 19), Ontario distributors have not earned their cost of equity in any year between 2015 and 2022. Even assuming that the authorized ROE itself met the Fair Return Standard, this reality provides clear evidence that the current Board cost of capital parameters as a whole are inconsistent with the FRS*." (page 81 – emphasis added)
And
"*Indeed, LEI provides evidence in its Figure 19 that the current regulatory approach in Ontario neither meets equity investor interests nor adheres to the FRS. Nexus concludes that a 3-year review period is a step toward ensuring that equity holders' interests are represented*." (page 83 – emphasis added)

30.1 Given that, at rebasing, Ontario electricity distributor's rates are set so as to incorporate the Board's cost of capital parameters, please explain how the fact Ontario electricity distributors have on average failed to attain their authorized return on equity demonstrates that the Board's cost of capital parameters are inconsistent with the FRS as opposed to a failure in some other aspect of the Board's current regulatory mechanisms.

30.2 How will more frequently reviewing and updating the cost of capital parameters better enable Ontario electricity distributors to attain their authorized ROE?

31.0 Reference: M3: NEXUS, page 82

Pre-amble: "*It is implausible to suggest that the average distributor in Ontario, over a period of 8 10 years, was unlucky or unskilled enough to fail to earn its required return on equity*."

31.0 In 2015 the Ontario Energy Board regulated 81 electricity distributors (OEB 2015-2016 Annual Report). In 2024 the OEB rate regulated only 58 electricity distributors (https://www.oeb.ca/ontarios-energy-sector/overview-energy-sector/energy-at-a-glance-by-the-numbers). Is it plausible that the consolidation of distributors in Ontario since 2015 was the result in whole or part due to unskilled utility management who were unable to earn the allowed rate of return

on equity? When calculating historical rates of return how did NEXUS adjust its analysis for utility consolidation over the last 8 year period (for example how an acquiring utility might have lower returns during a period of acquisition)?

31.1 What research has NEXUS undertaken which studies the reasons for under earnings in Ontario? Please provide any studies NEXUS has undertaken of the Ontario Distribution sector.

31.2 How many electricity distributors operated as “not for profit” in 2015 and how many continue to operate that way in 2024?

31.3 Is there any systemic difference between the achieved returns of Ontario electricity distributors by customer or rate base size (e.g.. <5,000 customers; 5,000-30,000 customers and >30,000 customers).

31.4 Is there any systemic difference between achieved returns of Ontario electricity distributors by location (e.g. northern Ontario, southwestern Ontario, Eastern Ontario and GTA)?

End of document