

**IN THE MATTER OF** the *Ontario Energy Board Act, 1998*,  
S.O. 1998, c. 15 (Schedule B);

**AND IN THE MATTER OF** a generic proceeding  
commenced by the Ontario Energy Board to consider the cost  
of capital parameters and deemed capital structure to be  
used to set rates

**RESPONDING SUBMISSIONS OF  
ELECTRICITY DISTRIBUTORS ASSOCIATION**

November 28, 2024

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## I. OVERVIEW

1. In its Closing Submissions dated November 7, 2024 (the “**EDA Closing Submissions**”), the EDA set out in considerable detail its recommendation for the Board’s determination of an authorized ROE for Ontario utilities.<sup>1</sup> The closing submissions of the other 13 parties raise little that the EDA did not already address in the EDA Closing Submissions. For that reason, and to avoid repetition, the responding submissions below focus on specific items that require additional correction, clarification, or context.

2. Overall, the critiques of some parties should not affect the Board’s confidence in Nexus’ analysis because it is data-driven, well-reasoned, neutral, justified, rigorous, and appropriate for the central goal of this proceeding, *i.e.*, to set a deemed ROE. The Board can also have confidence in the ROE proposed by Nexus because it has many commonalities with the expert evidence of others. Such commonalities are themselves evidence of a fair and reasonable ROE.

3. For clarity, the EDA’s decision not to address any point made by one of the other parties does not indicate its acceptance of that point.

## II. TWO POINTS OF CLARIFICATION ON THE EDA’S PARTICIPATION

4. Some of the other parties appear to misunderstand the EDA’s position about its focus on electricity distributors in this Generic Proceeding. The EDA represents Ontario electricity distributors, its interest in this proceeding relates to electricity distributors and, thus, it has only made a recommendation for a proposed ROE for application to electricity distributors. However, Nexus’ analysis was *not* limited only to distributors and instead considered utility companies

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<sup>1</sup> All defined terms not defined below have the meanings ascribed in the EDA Closing Submissions.

more broadly. The Board may, therefore, decide that Nexus' proposed ROE is relevant to other regulated utilities.

5. Also, parties that addressed Indigenous issues noted the silence from Nexus and other experts about these issues. The EDA respectfully acknowledges the importance of Indigenous interests in the electricity system, particularly in both generation and transmission development. For electricity distribution specifically, the EDA suggests that discussions regarding Indigenous participation be dealt with on a distributor-by-distributor basis.

### **III. SIMPLY AVERAGING ALL THE EXPERTS' PROPOSED DEEMED ROES IS METHODOLOGICALLY UNSOUND**

6. The Board Staff proposes that the Board address a complex situation by throwing up its hands and simply averaging the ROE figures proposed by all the experts. To do so would be unsound and is not a solution proposed by any of the experts. Crucially, it would not yield an ROE that satisfies the mandatory Fair Return Standard.

7. The Board has the admittedly daunting task of considering four experts' approaches to setting the proposed ROE, four sets of comparable proxy groups, four sets of data inputs, and 14 detailed submissions on how the Board should approach setting the deemed ROE for Ontario utilities. In that context, Board Staff recommends the Board simply "triangulate between the expert proposals."<sup>2</sup> But to do so without qualification would be an error, as that approach takes

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<sup>2</sup> Board Staff Submissions at 17-19.

each expert at face value and implies that all the experts' proposed approaches are as reliable which some are not.<sup>3</sup>

8. Board Staff's proposal to average all of the experts without qualification also unfairly tars Nexus and Concentric as mere "utilities' experts". They are not. Nexus has acted for both regulators and non-utilities in the past (as has Concentric).<sup>4</sup> Both applied independent analyses that reached different, though similar, conclusions.<sup>5</sup> There is no evidence that these well-respected experts biased their conclusions in favour of utilities. This contrasts with Dr. Cleary, who has repeatedly and intentionally represented only consumer interests in his drive to reduce ROEs in Canadian provinces. He admitted this reality on cross-examination.<sup>6</sup> Dr. Cleary uses subjective methodologies and inputs like the "bond yield plus risk premium" approach, his "usual" beta computed across 80 years for no logical reason, and a DCF growth rate that implies negative real growth. His views have not been accepted by other regulators.

9. Nonetheless, the thrust of Board Staff's proposal has some usefulness, which (if adjusted to address certain problematic expert evidence) is consistent with Nexus' proposed confidence interval approach. The EDA recognizes that there can be a range of reasonable approaches and decisions, but only to a point and with appropriate guardrails. For this reason, the EDA

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<sup>3</sup> Even the Board Staff's "stress-test" discussed in Board Staff Closing Submissions at 20-24 imports the flaws discussed elsewhere in this responding submission. These flaws include the Board Staff assuming that because there is no evidence of utilities experiencing issues attracting capital, the status quo must be working, and unfairly equating so-called "upward biases" in Nexus' and Concentric's opinions and an opposite downward bias in Dr. Cleary's opinion.

<sup>4</sup> See M3 Attachment, Zarumba Resume, M3 Attachment, Pampush Resume; see also Exhibit M2, Concentric Report, Appendix C.

<sup>5</sup> Dr. Pampush specifically confirmed on cross-examination that neither Nexus nor Concentric was involved in or had any discussions regarding the preparation of evidence of the other. See Transcript of Oral Hearing, Vol. 5 (2 October 2024), Toronto ("**Day 5 Transcript**") at 2:21-3:9.

<sup>6</sup> Transcript of Oral Hearing, Vol. 6 (10 October 2024), Toronto ("**Day 6 Transcript**") at 31:8-32:1, 114:1-10; Exhibit M4, Cleary Report at 29, 122.

recommends *the Board take confidence and comfort where experts' results are clustering together and conversely take caution where there are clear outliers*. Within a range of closely clustered results derived from sound methodological principles, averaging may be an appropriate final step to take into account small differences in approach; but without those qualifiers, averaging will mask important analytical flaws and outlier results.

10. If the Board agrees with the EDA's two corrections to LEI's proposed ROE approach described in the EDA Closing Submissions – considering the results of multiple methodologies and including a 0.5% transaction costs “adder” – then the proposed ROEs of Nexus (11.08%), Concentric (11.38%<sup>7</sup>), and LEI (10.4%) are clustered together and can be averaged. Dr. Cleary is the clear outlier (7.05%) and must be excluded.

11. That Dr. Cleary's ROE result is an outlier is unsurprising in light of his result-oriented and methodologically unsound approach. In some important respects, he uses personal opinion rather than economic principles. That fact cannot be ignored, and his analysis should not be included in any average among experts.

12. If Dr. Cleary's outlier ROE figure is excluded and LEI's methodology is conformed to the Board's 2009 ROE approach, averaging the closely clustered results of Nexus (11.08%), Concentric (11.38%), and corrected LEI (10.40%) yields an average ROE result of 10.95%. Such an approach would be an appropriate use of averaging if the Board wishes to incorporate multiple experts' perspectives. This deemed average ROE figure (10.95%) is in the range of

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<sup>7</sup> Once adjusted for leverage – see discussion at Transcript of Oral Hearing, Vol. 1 (25 September 2024), Toronto (“Day 1 Transcript”) at 106:6-11.

10.36% to 11.81% (Nexus' confidence interval), meeting the capital attraction, financial integrity, and comparable investment branches of the FRS.

13. Notably, the average proposed by Board Staff (between 8.79% to 9.32%) would put Ontario utilities substantially out of step with authorized ROEs in the comparable jurisdictions Nexus has highlighted, and indeed with most jurisdictions in North America, once adjusted for a common equity thickness.<sup>8</sup> This result would not satisfy the FRS comparable return requirement. And as confirmed by Concentric in response to a question by Commissioner Janigan, "the failure to meet one requirement of the fair return standard is likely to affect the other two over time."<sup>9</sup>

#### **IV. INTERVENORS' CRITIQUES OF NEXUS' PROPOSED ROE**

14. Grouped by subject, the EDA responds below to several critiques raised by the other parties.

##### **A. There is No Evidence Investors See U.S. Companies as Riskier than Ontario Utilities and an Absence of Evidence of Struggles to Raise Capital is Not Itself Evidence**

15. Several parties' closing submissions suggest that while there may be some integration in the North American capital market, investors still see U.S. companies as riskier than Canadian companies or have a "home bias" that would lead them to accept a lower ROE from an Ontario utility even where a higher ROE is available in the U.S. There is no such evidence, just speculation.

16. On this subject, Commissioner Janigan asked whether there is some adjustment that could be made to reflect this alleged difference in risk. *None of the experts* provided a proposal

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<sup>8</sup> Exhibit KP1.3, Nexus Presentation Day Slides at slide 4.

<sup>9</sup> Transcript of Oral Hearing, Vol. 4 (1 October 2024), Toronto ("**Day 4 Transcript**") at 119:23-27.

for how to make such an adjustment.<sup>10</sup> The Board does not have the evidence to make such an adjustment and should not make up its own adjustment.

17. As a result, the Board has to choose between accepting, for ROE comparison and calculation purposes, the ROEs of comparable North American utilities or rejecting them altogether. As detailed in the EDA Closing Submissions (and in the OEA closing submissions), the use of a North American comparable group is appropriate and commonplace in regulatory proceedings.<sup>11</sup> They should also continue to be used in Ontario.

18. The critique of using North American comparable ROEs largely rests on the circumstantial fact that the Ontario authorized ROE is and has been lower than average U.S. ROEs and no evidence has been presented that Ontario utilities have struggled to raise capital. One intervenor alleges that because “Ontario’s utilities have regularly earned their allowed [ROE], have raised capital on reasonable terms, and have maintained their financial integrity [...] most of the changes proposed by Nexus are unnecessary.”<sup>12</sup>

19. This conclusion cannot be given evidentiary weight (setting aside that it is factually incorrect because Ontario utilities have not regularly earned their allowed ROE according to a letter sent to the parties by Board Staff<sup>13</sup>), because many reasons could explain the lack of evidence of utility struggles to raise capital. Such reasons include that a utility may appear to be

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<sup>10</sup> Day 6 Transcript at 193:14-194:9.

<sup>11</sup> EDA Closing Submissions at paras 74-76; see also BCUC 2023 Decision at 16 and Alberta Utilities Commission Decision, 27084-D02-2023, “Determination of the Cost-of-Capital Parameters in 2024 and Beyond” (9 October 2023) at paras 99-104.

<sup>12</sup> CME Closing Submissions at paras 8-9.

<sup>13</sup> Ontario Energy Board Staff, *Generic Proceeding – Cost of Capital and Other Matters: Return on Equity Value Requests – Updated*, EB-2024-0063 (Ontario: Ontario Energy Board, 18 July 2024), attaching regulated and deemed ROE values.



financially secure until the point it is metaphorically “on fire;”<sup>14</sup> many Ontario utilities are owned by municipalities which can fund their utilities without recourse to the markets and mask financial difficulties, as compared to a commercial sector where issues become visible immediately;<sup>15</sup> the terms of any investment are unknown; and it is the *marginal* investor whose view impacts ROE even though other investors may still invest. The Board has no evidence before it that could help identify why there is no demonstrated inability to access capital despite the Ontario ROE being lower than its U.S. counterpart. The reality in Ontario is that any capital attraction problems are not observable, so it is speculative that the reason utilities do not report a capital attraction problem is because there is none. The Board cannot make a leap without evidence to say that Ontario utilities are, therefore, less risky than U.S. utilities.

20. Indeed, all the evidence points to the opposite conclusion. Together with the evidence referenced in the EDA Closing Submissions at paragraphs 74-75, and evidence on the same point cited by the OEA closing submissions at paragraph 89, Concentric cites evidence from the Economist Intelligence Unit which rates Canada and the U.S. both as A for overall country risk.<sup>16</sup> Similarly, Nexus cites the 2024 version of Aswath Damodaran’s “Country Default Spreads and 8 Risk Premiums”, which includes both U.S. and Canadian country risk at 0.00 percent.<sup>17</sup> In its closing submission, the OEA also pointed to country risk reports from Allianz indicating that both Canada and the U.S. were ranked AA1 as of January 2024.<sup>18</sup> Anecdotally in response to questions from counsel and Commissioner Janigan, Concentric pointed to its

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<sup>14</sup> Presentation Day Transcript at 58:6-13.

<sup>15</sup> This issue could be the subject of an amendment to the ARC if the Board wishes to consider it in the future.

<sup>16</sup> Exhibit M2, Concentric Report at 52.

<sup>17</sup> Exhibit M3, Nexus Report at 45, citing Aswath Damodaran, “Country Default Spreads and Risk Premiums” (5 January 2024), online: <[https://pages.stern.nyu.edu/~adamodar/New\\_Home\\_Page/datafile/ctryprem.html](https://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/ctryprem.html)>.

<sup>18</sup> OEA Closing Submissions at para 100.

discussions with Canadian pension funds and others that are investing in U.S. companies, see investments in either country as “fluid”, and preferring the higher U.S. returns.<sup>19</sup> And finally, Nexus provided evidence that Ontario utilities do not face less regulatory risks than their peers.<sup>20</sup>

21. U.S. and Canadian utilities are comparable in terms of *systemic* risk, with any differences reflecting only *idiosyncratic* risks that are offset by a diversified portfolio. AMPCO/IGUA’s closing submission refers to Dr. Pampush’s discussion of “an interesting concept of specific jurisdictional or utility risk being ‘diversifiable’ and thus cancelling out in a cost of equity analysis”. That “interesting concept” is the entire point of the CAPM methodology. Capital gets priced on the basis of *systemic* risk across an entire portfolio. Dr. Pampush explained the basis for this distinction on cross-examination of Nexus:

MR. MONDROW: Thanks. So investment in a lower-risk jurisdiction at a lower return than average for the market as a whole does not necessarily indicate a violation of the fair return standard; right?

DR. PAMPUSH: What exactly do you mean by a lower-risk environment? Because you can have -- that the way -- typically, the way capital gets priced is not on the basis of total risk; it's on systemic risk and not idiosyncratic risk. So you have to separate the total risk out into those two pieces before you can really determine whether it's getting priced out properly or not. And it's also, what you do with the muni is it has to be evaluated as though it were a stand-alone engine and not layered under the city ownership, itself. And then we look at the systematic risk associated with that type of asset.

MR. MONDROW: ***Do you think that all the regulatory jurisdictions in North America have the same risk?***

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<sup>19</sup> Transcript of Oral Hearing, Vol. 2 (26 September 2024), Toronto (“**Day 2 Transcript**”) at 147:8-151:23; Day 4 Transcript at 119:28-122:1.

<sup>20</sup> Exhibit M3, Nexus Report at 30-32.

DR. PAMPUSH: I doubt it, but I don't know. I have never evaluated it. *But that would be precisely the type of idiosyncratic risk that can get diversified away and therefore not priced into the cost of equity.*

MR. MONDROW: So, when you say it gets diversified away, what do you mean?

DR. PAMPUSH: What I mean is that there are certain risks that are unique to the asset, but, since they are not systemic to all of the assets in that class, you can maybe buy a holding in this one and one in that one, where they offset one another and essentially don't count.

...

What it is that, when you have -- let's say you invest in multiple assets that have different idiosyncratic risk. *Ultimately you put those in a portfolio, and your portfolio is big enough and diversified enough. Then, all of those risks basically disappear in the pricing model or just the way it's compensated, and the only thing that gets compensated is the variability of that portfolio's returns with the market as a whole.*<sup>21</sup> [Emphasis added]

22. For these reasons, it would be inappropriate, and based on no evidentiary foundation, for the Board to leave out North American comparables or import some arbitrary adjustment to the authorized ROE to reflect a risk differential that is at best, undeterminable, and at worst, non-existent, and is also idiosyncratic and diversifiable.

## **B. Alleged Flaws in Nexus' Approach to ROE**

### *(i) Selection of Comparables*

23. Some intervenors assert that Nexus' chosen proxy group is made up of companies that are not properly comparable to Ontario utilities for various reasons, including generation assets, unregulated revenues, or holding company structures.

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<sup>21</sup> Day 4 Transcript, 160:14-162:4; see also 190:16-196:4.

24. This issue is addressed in the EDA Closing Submissions at paragraphs 72-81. In repeating the EDA's prior comments, the reality is that the selection of a sufficiently broad group of publicly traded comparables is a critical component to modelling and determining ROE and that no comparable will be a perfect reflection of an Ontario utility. The alternative is having no proxy group at all, and then the Board is left without any basis for measuring whether the deemed ROE meets the FRS, a legal requirement.

25. While it is easy to choose a single comparable within a group of 45 companies and focus on the differences it specifically has from an average Ontario utility – as many intervenors did on cross-examination of Nexus and Concentric and as many of them again do in closing submissions – that is precisely the reason for having a larger proxy group and using *average* results that emerge from the group. For example, the growth rates and betas applicable to Otter Tail Corporation, which is one of the comparables attacked by the SEC,<sup>22</sup> are not being accepted at face value and applied to Ontario utilities. They are being factored into and averaged within an overall CAPM or DCF analysis, along with other comparables that may share more or less, or different, characteristics with Ontario utilities, *then* those results are being weighted according to their consistency with other economic models, *then* reasonableness and fairness of those cumulative results from all models are being compared to other jurisdictions' authorized ROEs to ensure comparability, and only *then* is the resulting ROE applied to Ontario utilities. In short: an averaging process offsets the effects of idiosyncratic differences,<sup>23</sup> and the use of multiple models provides a secondary level of confidence in results.

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<sup>22</sup> SEC Closing Submissions, section 2.3.

<sup>23</sup> N- M3-10-AMPCO/IGUA-36.

26. The allegations against Nexus' proxy group are unfounded. When Nexus reanalyzed its comparables using Concentric's screening criteria<sup>24</sup>, the results closely mirrored its original findings. Furthermore, the SEC's own analysis revealed minimal impact: When Concentric adjusted the comparables to address the intervenors' critiques, the proposed ROE decreased by only 0.27%, from 11.08% to 10.81%.<sup>25</sup> This marginal change falls well within the confidence interval established by Nexus, effectively undermining the criticisms leveled against Nexus' methodology.

27. Minor differences in approaches to creating a proxy group among experts are to be expected. As acknowledged by the BCUC, "the makeup of any proxy group inherently involves some degree of professional judgment and discretion."<sup>26</sup> Indeed, the fact that each of Nexus, Concentric, and LEI independently selected a proxy group (and Concentric selected multiple proxy groups) and all reached similar results shows the methodological rigour of their selection and the accuracy of the outcome.

28. Moreover, the critiques of Nexus' (and Concentric's and LEI's) proxy groups apply to a far greater degree when flipped against Dr. Cleary. At least three of his five comparables are susceptible to the identical exercise of identifying all the ways they are *unlike* Ontario utilities, with the added problem of having insufficient breadth to ensure such "less like" results are

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<sup>24</sup> Exhibit KP1.3, Nexus Presentation Day Slides at slide 18.

<sup>25</sup> SEC Closing Submissions at para 2.5.1.

<sup>26</sup> British Columbia Utilities Commission, G-236-23, "Generic Cost of Capital Proceeding Decision and Order" (5 September 2023) ("**BCUC 2023 Decision**") at 15-16.

averaged into a CAPM or DCF result. Even the SEC was forced to accept the need for a wider proxy group and so used Concentric's group, albeit with no expert evidence in support.<sup>27</sup>

*(ii) Use of U.S. Risk-Free Rate*

29. Some intervenors criticize Nexus' use of a U.S. risk-free rate in its CAPM analysis, stating that instead a Canadian rate should have been used, and for some intervenors, that an actual spot rate instead of a forecast rate should be used. This critique is misplaced.

30. Using a U.S. risk-free rate in this regard flows from Nexus' opinion that there is a single North American market for capital, and from Dr. Pampush's adherence to methodological consistency, that the U.S. risk-free rate must be used in a CAPM model that also uses a U.S.-inclusive MRP and beta.<sup>28</sup> As it concerns the use of a spot rate or a forecast rate, Nexus pointed out that it used a forecast to be consistent with the 2009 Board Report, but that a spot rate would not have materially impacted its CAPM analysis in any event.<sup>29</sup>

31. The propriety of Nexus' proposed risk-free rate is discussed at paragraphs 56-58 of the EDA Closing Submission.

*(iii) Use of Blume-adjusted betas*

32. While several parties' closing submissions reject using the Blume adjustment, the adjustment is well-established and warranted in this case, as explained in the EDA Closing Submissions at paragraphs 52-55. It is also worth noting that both LEI's and Concentric's raw

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<sup>27</sup> SEC Closing Submissions, section 3.5.

<sup>28</sup> EDA Closing Submissions at paras 56-58.

<sup>29</sup> N-M3-VECC 28(e); N-M3-10-AMPCO/IGUA-30.

beta numbers (i.e., without the Blume adjustment) are 0.69 and 0.89, respectively, the same as or higher than the Blume-adjusted average beta used by Nexus (0.69).<sup>30</sup> Similarly, Nexus points out that Damodaran’s 2024 industry sector beta for utilities, *without* the Blume adjustment, is a very similar 0.71.<sup>31</sup> Again, the clustering of results despite the uses of different approaches is a favourable indicator of accuracy.

(iv) *Use of MRP calculated based on DCF market growth*

33. While not directly attacking the merits of modelling a forward-looking MRP, some intervenors suggest that Nexus’ MRP is simply too high. As support, intervenors point to cited sources Blackrock, Kroll, and other predictors of market returns, and to expected and historical nominal GDP growth.<sup>32</sup> But Kroll and others have not laid out their MRP-calculation methodology for cross-examination and analysis, such that the Board simply has no way to know why Kroll apparently uses a 5-6% MRP.<sup>33</sup> The Board has no information about what is excluded and included in Blackrock, Kroll, and others’ MRP calculations. As a result, it has no way to compare, on a reliable and apples-to-apples basis, those MRPs with the MRPs proposed by the experts in this proceeding. The U.S. FERC has preferred expert evidence before it over the evidence of unsupported MRP calculations by financial analysts.<sup>34</sup> So should the Board.

34. In contrast to using black-box public MRPs, Nexus has presented a detailed, well-reasoned analysis in the form of an expert report, answered detailed interrogatories, and

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<sup>30</sup> Dr. Cleary’s beta is neither adjusted nor unadjusted, since he simply chose his “usual beta” and then applied an arbitrary adjustment upwards, not based on any actual comparable beta numbers.

<sup>31</sup> Exhibit M3, Nexus Report at 68; N- M3-10-OEB Staff-53.

<sup>32</sup> See an example, SEC Closing Submissions at para 4.2.20.

<sup>33</sup> Exhibit M1, LEI Report at 122.

<sup>34</sup> FERC Opinion 569 at paras 272-273.

withstood cross-examination to justify its forward-looking MRP of 8.83%. Further, Nexus' MRP of 8.83% is in line with the historical MRP of 8.32% computed by LEI and the overall average of historical and forward-looking MRPs of 9.06% computed by Concentric, this clustering again lending further credence to an MRP in that range.<sup>35</sup> (Dr. Cleary's biased 5% MRP is, once again, nowhere near the clustered results and not based on a credible analysis.)<sup>36</sup>

35. As stated in the EDA Closing Submission at paragraphs 46 – 50, calculating market return using a DCF analysis of the S&P 500 is a recognized approach recognized by other regulators.<sup>37</sup> It is appropriately used in this case in order to, as much as possible, model going-forward market conditions rather than resort to historical artifacts.

*(v) Single-stage DCF and growth rates*

36. Certain intervenors' closing submissions criticize Nexus' use of a single-stage DCF model rather than a multi-stage model, particularly its use of analyst-estimated growth rates for each of its proxy group companies over an indefinite time horizon. These criticisms are not new but are also all discussed and addressed in the EDA Closing Submission and other regulatory proceedings.

37. The EDA acknowledges that reasonable experts may disagree in a cost of capital proceeding about whether the single-stage or multi-stage approach is preferable: Nexus' view, as summarized in the EDA Closing Submission, is that "any theoretical benefits of [the multi-stage]

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<sup>35</sup> N-M3-10-AMPCO/IGUA-33; Exhibit KP1.3, Nexus Presentation Day Slides at slide 19.

<sup>36</sup> N-M3-10-AMPCO/IGUA-33; Exhibit KP1.3, Nexus Presentation Day Slides at slide 19.

<sup>37</sup> FERC Opinion 569 at paras 260-266.



approach are mitigated by its implementation challenges”<sup>38</sup>, which include all of the assumptions and analyst intervention a multi-stage analysis inherently requires, leading to opportunities for engineered results or errors.

38. It is also not uncommon to question whether sell-side analyst forecasts are reliable or bear any “optimism bias”, although Nexus and Concentric have both provided conclusive evidence there should be no such concern undermining their use in this case.<sup>39</sup>

39. In short: the EDA continues to endorse a proposed ROE incorporating the results of Nexus’ DCF model as-performed (10.92%), but the Board may also wish to average the results of other reasonable DCF models reaching closely clustered results, like LEI’s (10.77%), to have the benefit of different perspectives on the issues identified above. The EDA would also consider that to be a reasonable approach.

40. Reasonable experts disagree that growth estimates *cannot* be below nominal GDP (as proposed by Dr. Cleary). The AUC also disagrees because it would lead to negative real growth and “over the long term investors would not accept the risks of equity ownership if the expected long-term outlook for real growth was at or near negative levels.”<sup>40</sup> Therefore, Dr. Cleary’s

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<sup>38</sup> EDA Closing Submissions at para 61.

<sup>39</sup> See Exhibit M3, Nexus Report at 53-54, 69-72, and Exhibit M2, Concentric Report at 59-60. Further, average analyst estimates of utility earnings per share growth used by Nexus (7.11%) are very close to historical nominal GDP growth rates in the U.S. (6.4% per year over the period from 1950 to 2023) and Canada (7.06% per year over the period from 1961 to 2023) over the long term. Since the DCF is estimated over the very long term, the long-term historical growth rate and the forward-looking analyst rates are consistent with one another. This GDP growth data is pulled from the St. Louis Federal Reserve and is available at the following web addresses for U.S. and Canada, respectively:

- <https://fred.stlouisfed.org/series/NGDPXDCUSA>; and  
- <https://fred.stlouisfed.org/series/NGDPSAXDCCAQ>.

<sup>40</sup> Alberta Utilities Commission Decision, 22570-D01-2018, “2018 Generic Cost of Capital, Proceeding” (2 August 2018) at para 439.

model should not be incorporated into any averaging exercise due to its inclusion of an unacceptably low growth rate.

(vi) *Use of U.S. authorized ROEs in risk premium analysis*

41. Certain intervenors criticized Nexus for using authorized ROEs in its risk premium analysis instead of actual earned ROEs, calling them “not market data”. The EDA acknowledges this critique, but as pointed out by Nexus, “authorized returns represent the returns on equity capital that Ontario electric utilities compete with. Under the Fair Return Standard’s opportunity cost standard, the authorized returns provide relevant evidence that should be considered.”<sup>41</sup> Authorized ROEs are appropriately used when setting and benchmarking a deemed ROE, recognizing that actual returns may under-achieve against an authorized ROE for various reasons unrelated to what number is fair and required to compensate the company.

42. In any event, Nexus assigned its risk premium figure only a 13% weight in its ultimate ROE recommendation. Therefore, it has little overall impact. Moreover, the 11.09% risk premium figure is very close to Nexus’ ultimate proposed ROE (11.08%), so any critique of the Nexus risk premium approach does not move the needle on the deemed ROE.

**C. Ownership of Utilities is Irrelevant to Authorized ROE**

43. A surprising issue raised in various parties’ closing submissions is their endorsement of an approach to setting authorized ROE based on municipal ownership of the utility. While masked in some cases as a basis for differentiating U.S. utilities from Canadian utilities, ownership is irrelevant. In an integrated market (which the North American market is, as

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<sup>41</sup> N-M3-10-AMPCO/IGUA-36(b).

explained above and acknowledged in theory by other parties<sup>42</sup>), idiosyncratic differences such as ownership are diversifiable.<sup>43</sup>

44. Taking into account ownership was not supported by *any* of the experts, including Dr. Cleary.<sup>44</sup> Further, setting an Ontario ROE based on the ownership of Ontario utilities conflicts with the 2009 Board Report and violates the FRS.<sup>45</sup> As stated by Nexus, the cost of capital depends on the use of funds, not the source of the funds: “There will be a single price for risk-free assets, and a single price for risky assets of the same or comparable riskiness.”<sup>46</sup>

#### **D. Any “Opportunity” Presented by Energy Transition Does Not Decrease Risk**

45. While some intervenors suggest that the energy transition is a factor decreasing rather than increasing risk to utilities, this point is incorrect and misunderstands the nature of risk. The EDA has already commented on how the energy transition ought to factor into the Board’s analysis at paragraphs 29 – 35 of the EDA Closing Submissions.

46. To respond specifically to the argument that the energy transition reduces risk for electricity distributors, importantly, *no* party has presented any evidence in this regard; instead, this argument rests on the flimsy premise that more demand must equal more money and, thus, less risk. This is speculative and intellectually flawed for the reasons already explained in the EDA Closing Submission.

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<sup>42</sup> See OEA Closing Submissions at paras 89, 138; notably, SEC Closing Submissions at para 2.5.6 also concedes an integrated North American market.

<sup>43</sup> Day 1 Transcript at 151:1-12.

<sup>44</sup> See Day 6 Transcript at 33:16-34:27; Day 1 Transcript at 114:6-17.

<sup>45</sup> Ontario Energy Board, EB-2009-0084, “Report of the Board on the Cost of Capital for Ontario’s Regulated Utilities” (11 December 2009) (“**2009 Board Report**”) at 25-26; see Closing Submission at para 27(a).

<sup>46</sup> Exhibit M3, Nexus Report at 45; see also discussion on Day 4 Transcript at 156:4-163:10.

47. Unlike the dearth of evidence presented in support of this critique, Nexus, and Concentric provided concrete evidence that the energy transition is happening and is increasing risk for Ontario utilities.<sup>47</sup> Several of Dr. Cleary's comparable companies (Fortis, Emera, and Algonquin) explicitly identify risks in their Annual Reports associated with the energy transition.<sup>48</sup> And as pointed out by Nexus, the major risk associated with the energy transition is that demand does not materialize as projected, and distributors are left with the infrastructure they had to build but no longer require.<sup>49</sup>

48. In any event, as Nexus has stated repeatedly, it made no adjustment to its proposed ROE to reflect any risk associated with the energy transition. The EDA's proposed 11.08% figure flows from Nexus' application of well-established and principled models as described in the EDA Closing Submission.

#### **E. Transaction Costs Should Remain an Adder in Authorized ROE**

49. In what can be interpreted only as a transparent attempt to encourage a lower authorized ROE, AMPCO/IGUA flatly contradicts the evidence and recommendation of their own expert to contend that the 0.5% transaction costs "adder" should be removed from the authorized ROE.<sup>50</sup>

50. AMPCO/IGUA also submits – based on no evidence from Dr. Cleary or anywhere else – that since 0.5% has been recovered as part of the authorized ROE "for some years", "it would be reasonable for the OEB to assume that these recoveries have reasonably compensated the utilities

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<sup>47</sup> While the EDA takes no position on issues affecting natural gas utilities, the SEC's suggestion in SEC Closing Submissions at para 3.2.2 that natural gas utilities and electricity utilities cannot *both* face risks from the energy transition – perhaps different in nature – is absurd.

<sup>48</sup> Exhibit K6.2, Tabs 18-21.

<sup>49</sup> Day 5 Transcript at 36:4-22; Exhibit M3, Nexus Report at 27-28.

<sup>50</sup> AMPCO/IGUA Closing Submissions at paras 79-80.

for any historical equity financing costs.”<sup>51</sup> The EDA disagrees this would be a reasonable assumption, and in fact, the explicit evidence of Nexus goes the other way: amortization of transaction costs into infinity to reach a 0.5% adder means that the company will never recover all of its transaction costs.<sup>52</sup>

51. The rationale for continuing to include transaction costs in the authorized ROE is set out in the EDA Closing Submission at paragraphs 85–96. Contrary to the Board Staff’s characterization of transaction costs as a “benefit”<sup>53</sup> that should not accrue to utilities that do not incur them is incorrect; in an exercise of modelling the *deemed* cost of capital, irrespective of ownership, transaction costs are a component of that cost that needs to be deemed along with the rest.

52. The EDA urges the Board to ask itself a simple question when weighing whether elimination of the transaction costs adder is appropriate: Is there anything that has changed since the 2009 Board Report that would warrant a departure from the practice established by the Board and other Canadian regulators, relied upon by Ontario utilities and their investors? The answer is, unquestionably, no. Since nothing has changed in this regard, this adder should also not change. Moreover, the Board should not artificially divorce this single cost component from the deemed cost of capital model otherwise applicable to Ontario utilities. All costs of capital, including transaction costs, should be treated in the same manner, as they have been for many years in Ontario.

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<sup>51</sup> AMPCO/IGUA Closing Submissions at paras 79-80.

<sup>52</sup> Day 4 Transcript at 140:20-141:4.

<sup>53</sup> Board Staff Closing Submissions at 24.

**V. CONCLUSION**

53. The EDA again respectfully submits that its proposed deemed ROE of 11.08% is a just and reasonable result that the Board should authorize. However, to the extent that the Board wishes to incorporate other methodologically sound and closely clustered results into its authorized ROE through an averaging exercise, it must be informed by the comments set out in this responding submission in order to achieve a proposed ROE of 10.95% that also adheres to the FRS.