CME, CCC, SEC, VECC INTERROGATORY #11

INTERROGATORY

E - Cost of Capital
Issue E2: Is the proposed change in capital structure increasing Enbridge's deemed common equity component from 36% to 42% appropriate?

Reference: EGDI Evidence E2, Tab 2, Schedule 1, report of Concentric Energy Advisors.

At pages 22 to 27, Concentric discusses credit ratings and provides its hypothetical credit ratings for EGDI. At pages 28 to 30, Concentric compares equity ratios among North American gas distribution utilities.

a) Please identify any Canadian regulator that has “set a goal of the lowest possible investment grade credit rating” in the context of the discussion on page 22.

b) Please provide any precedent decisions where a regulator relied on hypothetical rather than actual credit ratings in determining utility equity ratios.

c) Please provide the full data used to generate the graph on page 27 in machine readable Excel format so that the graph can be replicated.

d) Given the lower common equity ratios of the Canadian utilities shown in Figure 7 on page 31, compared to the US utilities, please explain why all of the Canadian utilities have good investment grade bond ratings.

e) Please confirm that the costs of debt recoverable from EGDI ratepayers should be unaffected by any future S&P downgrades attributable to problems at EGDI’s holding company.

RESPONSE

a) Concentric is not aware of any Canadian regulators that have “set a goal of the lowest possible investment grade credit rating”. The point of the referenced statement is that with each reduction in credit rating, or with increased financial risk, financial flexibility is further impaired.

Witnesses: J. Coyne
J. Lieberman
Concentric

b) Concentric is not aware of any precedent decisions where a regulator has not considered the potential or "hypothetical" credit rating impact of its equity ratio decisions. However, Concentric is aware of no regulatory decisions that have been based entirely on credit ratings either hypothetical or actual credit ratings.

c) The excel file will be distributed electronically to intervenors following the filing of the interrogatory responses with the Ontario Energy Board.

d) Not all Canadian utilities have good credit ratings. For example, PNG had a below investment grade credit rating in 2000 and 2001, and has been rated at the lowest investment grade since 2003.[1] However, Concentric acknowledges that Canadian utilities do typically enjoy a solid investment grade credit rating. This may be due in part to a large portion of Canadian electric utilities that are government owned and enjoy the benefit of the good credit of the government. Additionally, most Canadian regulatory jurisdictions are deemed by the ratings agencies to be very supportive of credit quality. Both factors weigh heavily into ratings agency decisions.

e) Concentric agrees that the costs of debt recoverable from EGDI ratepayers would not be immediately affected by a future S&P downgrade attributable to problems at EGDI's holding company. However, ratings agencies link the ratings of the holding company and its affiliate companies. If there were a downgrade at the holding company level, depending upon the level of ring fencing in place at the utility level, EGDI ratepayers may share in the effects of the downgrade and EGD may be subject to a down grade itself and as a result, higher debt costs. Though this would not impact the coupon payment on outstanding debt, it may trigger debt covenants and enhanced collateral requirements for existing debt as well as subjecting the utility to higher debt costs and more stringent terms for future financings.

[1] Bloomberg

Witnesses: J. Coyne
J. Lieberman
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