STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: NARRAGANSETT ELECTRIC	:	
COMPANY d/b/a NATIONAL GRID	:	**DOCKET NO. 4065**

THE DIVISION OF PUBLIC UTILITIES AND CARRIERS
RESPONSE TO THECOMMISSION'S THIRD DATA REQUEST

3-1. Please provide an itemized list of the costs the Division expects to bill NGrid in relation to Docket 4065.

Response:

The following is a listing of expense incurred to date, including an estimate of unbilled costs projected to be billed to the Division through the case conclusion.

Total of consultants/expert witnesses:	$225,583
Stenographers	12,000
	$237,583

The amount shown above represents what has been billed to the Division, as well as what we anticipate will be billed through the end of the case. Under State law, when the Division bills utilities for reimbursement of costs of the Division or Commission, we are required to increase our bills by 11% for remittance to the State of RI general fund. Therefore the amount of $237,000 shown above would have to be increased to $263,000 to reflect what the Division would have to bill National Grid to recover its costs and remit the required amount to the state general fund.

Response provided by Stephen Scialabba

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2. Does a change in capital structure affect the mechanics of the DCF calculation?

Response

Generally speaking, a change in capital structure does not alter the mechanics of the DCF analysis used to determine the applicable cost of equity. If the proposed capital structure differs markedly from the DCF proxy group average capital structure, then such difference may warrant an adjustment to the proxy group DCF finding. However, if such an adjustment is deemed appropriate, this would be an external adjustment after the DCF analysis has been completed. It is not part of the DCF "mechanics" itself.

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3. If the RI Commission were to approve a capital structure for Narragansett Electric that consisted of 38% equity and 62% debt, what effect, if any, would that have on the Division's recommendation for an appropriate ROE.

Response

The Division has not conducted a formal analysis of the cost of equity implications of a 38/62 capital structure. However, since this capital structure differs significantly from that assumed by the Division (and implicit in the Division's two proxy groups), it is possible that the Division would modify its return on equity recommendation above the 10.1 percent current figure. For example, the upper end of Staff's DCF range is 10.45 percent, and a figure toward this upper end may be a more reasonable award than the 10.1 percent midpoint if the ratemaking capital structure is determined to be 38 percent equity/62 percent debt. The 10.45 percent is the average of the electric proxy group upper bound DCF of 10.7 percent and the gas proxy group DCF upper bound of 10.2 percent. (See Schedules MIK-4 and 5, page 1 of 4.)

In evaluating a revised range of 10.1 to 10.45 percent in conjunction with a 38/62 capital structure, the Commission may wish to consider additional factors:

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<u>Data Response No. 3</u> (Cont'd)

- The CAPM produces cost of equity estimates lower than the DCF.
- The Division's cost of equity DCF studies used market data through August 2009. Equity markets have improved since then.
- While the Division's proxy companies have capital structures less leveraged than 38/62 equity debt, as posed in the question, some of these proxy companies have riskier non-regulated operations. Inevitably, some of that additional risk is captured in the DCF calculations.

For these reasons, the Commission should consider a return on equity range of 10.1 to 10.45 percent if it adopts a 38/62 capital structure, but no higher than 10.45 percent.

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