


Slide 1



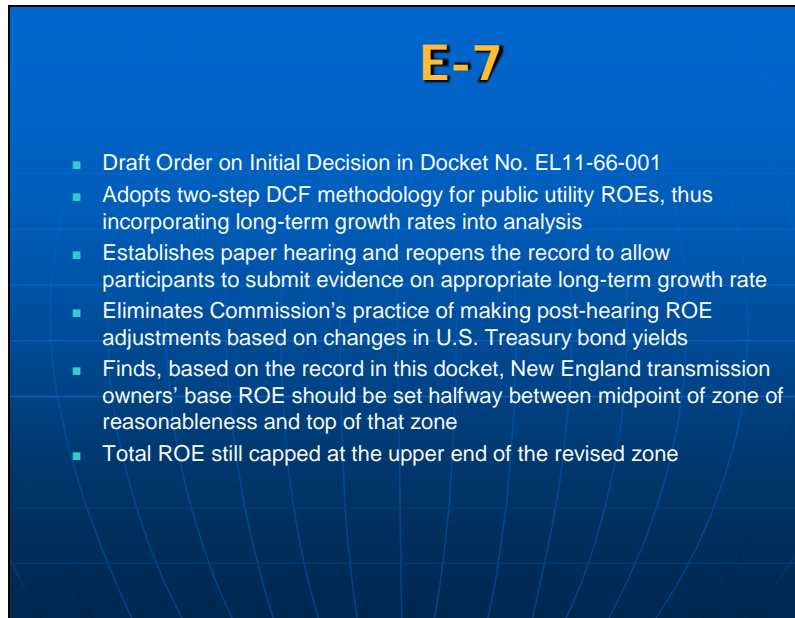
**Return on Equity
(ROE)**

Item No's: E-7, E-8, E-9, E-10,
E-11, E-12, E-24

Meeting Date: June 19, 2014

Good morning, Madame Chairman and Commissioners.

Slide 2

The slide features a blue background with a grid pattern. At the top center, the text "E-7" is displayed in a large, bold, orange font. Below this, a list of seven bullet points is presented in white text, each preceded by a small orange square. The bullet points describe a draft order regarding public utility ROEs, including details on methodology, hearings, and specific findings for New England transmission owners.

E-7

- Draft Order on Initial Decision in Docket No. EL11-66-001
- Adopts two-step DCF methodology for public utility ROEs, thus incorporating long-term growth rates into analysis
- Establishes paper hearing and reopens the record to allow participants to submit evidence on appropriate long-term growth rate
- Eliminates Commission's practice of making post-hearing ROE adjustments based on changes in U.S. Treasury bond yields
- Finds, based on the record in this docket, New England transmission owners' base ROE should be set halfway between midpoint of zone of reasonableness and top of that zone
- Total ROE still capped at the upper end of the revised zone

E-7 is a draft order affirming in part and reversing in part an initial decision concerning the New England Transmission Owners' base return on equity as provided for in ISO New England's tariff. The draft order changes the Commission's approach to determining the base return on equity for public utilities, applies this approach to the facts of this proceeding, and institutes a paper hearing to allow the participants an opportunity to submit evidence on a limited issue concerning the application of this approach in this proceeding.

Historically in public utility rate cases, the Commission has used a one-step discounted cash flow methodology to determine a public utility's base return on equity. The draft order changes the Commission's approach by adopting for public utilities the two-step discounted cash flow methodology that the Commission uses to determine the return on equity for natural gas pipelines and oil pipelines. The difference between the one-step and two-step discounted cash flow methodologies is that the one-step methodology relies on short-term growth rates, whereas the two-step methodology incorporates both a short-term and a long-term growth rate estimate. In natural gas and oil pipeline cases, the Commission uses gross domestic product, or GDP, as the long-term growth rate estimate.

The draft order applies the two-step discounted cash flow methodology to this proceeding, tentatively using GDP as the long-term growth rate estimate, but directs a paper hearing to allow participants to present evidence on the appropriate long-term growth rate to use in applying the two-step discounted cash flow methodology in this case. Further, while the Commission typically places the base return on equity at

the central tendency of the zone of reasonableness produced by a discounted cash flow analysis, the draft order finds, based on the record in this proceeding -- including the existence of unusual capital market conditions -- that placement of the base return on equity halfway between the midpoint of the zone of reasonableness and the top of that zone results in a just and reasonable rate. Applying this analysis, and subject to the long-term growth rate set for hearing, the draft order tentatively finds that a just and reasonable base return on equity for the New England Transmission Owners is 10.57 percent.

The draft order also eliminates the Commission's past practice of using U.S. Treasury bond yields to make a final adjustment to a public utility's base return on equity to reflect changes in capital market conditions after the close of the record in a hearing proceeding. The draft order explains that there is not necessarily a one-to-one correlation between U.S. Treasury bond yields and public utility returns on equity. The draft order instead allows participants in a rate case to present at their hearing the most recent financial data available at the time of the hearing, including post-test period financial data then available. This approach ensures that all participants have an opportunity to present evidence and arguments concerning the financial data used to determine the public utility's return on equity, while allowing the return on equity to be based on the most recent financial data available at the time of the hearing, consistent with the due process rights of the participants.

Finally, the draft order indicates that a utility's total ROE will still be capped at the upper end of the revised zone.

E-8, E-9, E-10, E-11, E-12

- Draft orders address complaints challenging public utility ROEs
- Draft orders establish hearing and settlement judge procedures
- Draft orders note changes in the Commission's approach set forth in E-7 and indicate that the Commission expects the evidence and any DCF analysis presented by the participants be guided by the decision in E-7

Items E-8, E-9, E-10, E-11, and E-12 are draft orders setting for hearing and settlement judge procedures other complaints challenging public utilities' base return on equity. Those draft orders indicate that the Commission expects the evidence and any DCF analyses presented by the participants in these other proceedings be guided by our decision in E-7.

E-24

- Draft order on Remand from D.C. Circuit
- Draft order notes the change in approach announced in E-7 concerning post-hearing ROE adjustments; draft order reverses a 2010 Commission decision to apply the U.S. Treasury bond yield adjustment to Southern California Edison Company's ROE

Item E-24 is a draft order reversing a prior Commission decision on remand from the United States Court of Appeals for the D.C. Circuit, involving an order in which the Commission made a U.S. Treasury bond-based post-hearing adjustment to Southern California Edison Company's return on equity. As in E-7, the draft order in E-24 explains that the Commission is changing its practice in public utility cases to no longer make post-hearing adjustments to the return on equity based on changes in U.S. Treasury bond yields. Accordingly, the draft order reverses the Commission's previous decision to make such an adjustment to Southern California Edison Company's return on equity.

Thank you. We are happy to answer any questions you might have.