

PEPCO (B)

POTOMAC ELECTRIC POWER COMPANY

BEFORE THE
PUBLIC SERVICE COMMISSION OF DISTRICT OF COLUMBIA
DIRECT TESTIMONY OF DR. ROGER A. MORIN
FORMAL CASE NO. ____

1 Q. PLEASE STATE YOUR NAME, ADDRESS, AND OCCUPATION.

2 A. My name is Dr. Roger A. Morin. My business
3 address is Georgia State University, Robinson College
4 of Business, University Plaza, Atlanta, Georgia,
5 30303. I am Professor of Finance at the College of
6 Business, Georgia State University and Professor of
7 Finance for Regulated Industry at the Center for the
8 Study of Regulated Industry at Georgia State
9 University. I am also a principal in Utility Research
10 International, an enterprise engaged in regulatory
11 finance and economics consulting to business and
12 government.

13 Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND.

14 A. I hold a Bachelor of Engineering degree and an
15 MBA in Finance from McGill University, Montreal,
16 Canada. I received my Ph.D. in Finance and
17 Econometrics at the Wharton School of Finance,
18 University of Pennsylvania.

19 Q. PLEASE SUMMARIZE YOUR ACADEMIC AND BUSINESS CAREER.

20 A. I have taught at the Wharton School of Finance,

Witness Morin

1 **III. SUMMARY OF COST OF EQUITY RECOMMENDATION**

2 Q. PLEASE SUMMARIZE YOUR RESULTS AND RECOMMENDATION.

3 A. To arrive at my final recommendation, I performed
4 four risk premium analyses. For the first two risk
5 premium studies, I applied the CAPM and an empirical
6 approximation of the CAPM using current market data.
7 The other two risk premium analyses were performed on
8 historical and allowed risk premium data from electric
9 distribution industry aggregate data. I also
10 performed DCF analyses on two surrogates for Pepco: a
11 group of investment-grade electricity distribution
12 utilities and a group of representative of the natural
13 gas distribution utility industry.

14 The average result from the three principal
15 methodologies is as follows:

17	CAPM	11.9%
18	Risk Premium	11.1%
19	DCF	10.2%
20	AVERAGE	11.0%

21 The overall average result is 11.0% for the
22 average electricity distribution utility. Note that
23 all three methods, including DCF are equally weighted,
24 and that the DCF results are based on four different

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1 tests.

2 Q. THE COMPANY HAS PROPOSED A BILL STABILIZATION
3 ADJUSTMENT THAT WILL PROVIDE MORE ASSURANCE OF
4 ACHIEVING THE AUTHORIZED LEVEL OF REVENUE SET IN THIS
5 CASE. IF ADOPTED BY THE COMMISSION, DOES THIS
6 MECHANISM HAVE ANY EFFECT ON THE RATE OF RETURN ON
7 EQUITY THAT YOU WOULD RECOMMEND?

8 A. Yes, I believe it would. If the proposed BSA
9 mechanism, discussed by other witnesses in this
10 proceeding, is approved, the Company's risk will be
11 reduced, and the cost of common equity capital will
12 likely decline by some 25 basis points from 11.00% to
13 10.75%. This assessment is based on bond yield
14 differentials and beta risk differentials, as
15 previously discussed.

16 Q. DR. MORIN, WHAT IS YOUR FINAL CONCLUSION REGARDING
17 PEPCO'S COST OF COMMON EQUITY CAPITAL?

18 A. Based on the results of all my analyses, the
19 application of my professional judgment, and the risk
20 circumstances of Pepco, it is my opinion that a just
21 and reasonable return on the common equity capital of
22 Pepco's electricity distribution operations in the
23 District of Columbia at this time is 11.00%.

24 Q. DR. MORIN, WHAT CAPITAL STRUCTURE ASSUMPTION UNDERLIES