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Witness: Brendan J. O'Brien and Garrett J. Murray
Request from: Office of Consumer Counsel

Question:

(WACC) Did the Company do any weighted average cost of capital analysis (WACC) which compared various debt percentages compared to equity. Such as 60% debt to 40% equity, 55% debt to 45% equity, and 40% debt to 60% equity.

Response:

There is no "test" that the Company can apply to try out different equity ratios in the capital structure relating to the weighted average cost of capital, such as 60% debt/40% equity, 55% debt/45% equity, or 40% debt/60% equity. The Company's capital structure reflects the actual capitalization of the Company, which is a critical input to the credit-rating process. To "test" out the effect of various capital structures on the Company's credit-rating outcome, it would be necessary to issue actual debt at different levels and see how the credit-rating agencies react, which means that the results of the "test" could be an actual credit action that the Company cannot then pull back.

The response below references Moody's June 30, 2026 credit opinion for the Company, provided here as OCC-757, Attachment 1.

The Company is proposing to use actual capital structure for determining the weighted average cost of capital (as adjusted for known financing activities) in order to reflect the financial realities of providing distribution service in Connecticut and the importance of maintaining credit quality to support ongoing access to capital on reasonable terms.

Although increasing debt may appear to reduce WACC in a purely arithmetic sense, capital structure decisions must also account for the effect of leverage on financial risk, credit quality, and long-term financing costs. In the Company's circumstances, maintaining an equity ratio of 53.86% supports the Company's ability to attract capital on reasonable terms and continue making the substantial investments required to provide safe and reliable electric distribution service. Accordingly, the Company's actual capital structure reflects a balance between financing costs and financial strength, rather than the results of a simple debt-versus-equity sensitivity analysis.
CL&P's capital structure should enable the Company to maintain or enhance financial integrity, thereby enabling access to capital at competitive rates under a variety of economic and financial market conditions.

As a regulated utility that relies on constant access to capital markets in order to finance necessary infrastructure investments, the Company does not have the option to avoid raising external funds during periods of capital market distress. Capital-intensive companies are financed in light of the risks and funding requirements associated with their assets and operations. Additionally, companies operating within a given sector are likely to have comparable financing requirements, face common financing constraints and, therefore, have comparable financing practices. As such, CL&P assesses its capital structure relative to prevailing industry practice, as compared to other utilities with similar financing requirements and business risks.

Currently, CL&P has a target capital structure with an equity ratio of approximately 53% to 54%. CL&P's assessment of its operating environment is that an equity ratio of approximately 53% to 54%, is consistent with those in place at other similar utilities and is necessary to enable the Company to maintain or enhance its financial integrity thereby providing access to capital at competitive rates under a variety of economic and financial market conditions. As noted in Exhibit CLP-ROE-1, Ms. Bulkley noted that CL&P's proposed equity ratio of 53.86 percent is well within the range of equity ratios of the utility operating subsidiaries of the proxy group, as supported by her capital structure analysis presented in Exhibit CLP-ROE-12.

In addition, as recognized by Moody's in its June 2026 report, the Company's credit profile remains heavily influenced by the Connecticut regulatory environment. Moody's stated that it would consider an upgrade if "the credit supportiveness of the Connecticut regulatory environment substantially improves with future regulatory decisions that are more predictable and enhance the timeliness of the recovery of costs and investments. In addition, an upgrade could be considered if we expect CL&P will be able to sustain a stronger financial profile on a consistent basis, including a ratio of CFO pre-WC to debt of 20% or higher." (OCC-757, Attachment 1, page 3) Moody's further stated that the Company "could be downgraded if Connecticut regulatory decisions continue to be contentious or unsupportive of credit quality or ***if CL&P's financial performance deteriorates such that its ratio of CFO pre-WC to debt falls below 17% on a sustained basis***." (OCC-757, Attachment 1, page 3, emphasis added)

A capital structure reflecting a 60% debt ratio, while holding other key assumptions constant, including assuming the Company's proposed 10.25% return on equity is approved in this proceeding as filed, would produce a Moody's CFO pre-working capital to debt ratio approaching 15% for the distribution business. That level would fall materially below the 17% threshold identified by Moody's as a potential basis for downgrade and would remain below that threshold beyond Rate Year 1.