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Request from: Public Utilities Regulatory Authority

Question:
(Common Equity) Application, Att. A, pp. 15−16. Explain why the Company maintains a regulatory equity ratio of 53.86%. What is the basis for the targeted equity ratio and explain the process by which the common equity component will be achieved?

Response:

The Company maintains a regulatory equity ratio of 53.86% because this is the level of equity capitalization that the Company perceives is necessary to maintain adequate credit ratings to support the business and deliver a reasonable cost of capital to customers, given what the Company's obligations are for financial stability. CL&P's assessment of its operating environment is that an equity ratio of approximately 53.86% is consistent with those in place at other similar utilities and is appropriate to enable the Company to maintain its financial integrity thereby providing access to capital at competitive rates under a variety of economic and financial market conditions.

Utilities have a public service obligation to provide safe and reliable service to customers, and require the ability to access capital markets in the provision of that service. In addition, utilities generally do not have the option to avoid raising external funds during periods of capital market distress. Capital-intensive companies are financed with a view on 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. For this reason, CL&P assesses its capital structure relative to prevailing industry practice, as compared to other utilities with similar financing requirements and business risks.

The Company is also focused on the role capital structure plays with respect to its credit ratings. The credit rating agencies view capital structure as a pivotal element in their analytical construct. For example, 50 percent of Moody's overall ratings weight is derived from Moody's assessment of Regulatory Framework and Ability to Recover Costs and Earn Returns. An appropriate level of equity capitalization is a critical element of this analysis. In addition, the Moody's Ratings Methodology gives Capital Structure a 7.5% weighting for the rating. The Company's target capital structure of 53.86% is supportive of the Company's credit ratings, which provide benefits to customers in the form of reasonable capital costs and assured liquidity. Lastly, the Company

has met this threshold for a credit-supportive capital structure for many years and changes to this structure attempted by the Company (or imposed by a regulatory outcome) would be detrimental to the Company's efforts to show financial and regulatory stability in the Connecticut regulatory environment.

In order to achieve its target equity ratio of 53.86%, CL&P will coordinate its proposed 2026-2027 long-term debt issuances with the timing and amount of earnings, capital contributions from Eversource Energy, and dividends to Eversource Energy.