Case 07-E-0949
Exhibit___(FP-1)

State of New York
Department of Public Service

Orange & Rockland Utilities, Inc.
Case No. 07-E-0949

Information/Document Request

Request No.:	DPS-87
Requested By:	Michael J. Augstell (518) 486-2874
Date of Request:	11/01/07
Reply Date:	11/11/07
Witness:	Roger A. Morin
Subject:	DCF Methodology

On page 8, line 8 through line 11, of his testimony, Dr. Morin states that it is the cost of capital for O&R's electric utility business that must be determined and not the cost of capital of the consolidated parent company.

(1) In his DCF methodology, does Dr. Morin use the parent company or the utility subsidiaries in his proxy groups?

(2) Provide the current bond ratings and Standard & Poor's business profile scores for the companies used in Dr. Morin's proxy groups.

(3) On average, are the bond ratings of the companies used in Dr. Morin's proxy groups higher or lower than Orange & Rockland's bond rating?

(4) On average, are the business profile scores for the companies used in Dr. Morin's proxy groups higher or lower than Orange & Rockland's business profile score?

(5) What percentage of the companies in Dr. Morin's proxy groups own electric production assets?

(6) Does Dr. Morin view electric production assets as riskier than electric distribution assets?

(7) For Dr. Morin's proxy groups, what percentage, on average, of revenues are derived from non-utility businesses?

(8) Does Dr. Morin view non-utility business risk as higher or lower than Orange & Rockland's electric division's business risk?

(9) In Dr. Morin's view, are the risks of the parent companies in Dr. Morin's proxy groups equal to, less than, or greater than the risks of Orange & Rockland's electric utility business? Explain.

RESPONSE:

1) Dr. Morin's testimony calculates the cost of equity for the operating companies using the market data of the consolidated parent companies as a proxy. This technique is required because the operating companies do not have publicly traded common stocks.

2) See attached extract from AUS Utility Reports November 2007 edition and S&P Report for the business profile scores.

3) See AUS Utility Reports November 2007 edition attached in respoinse to 2). The sample was carefully constructed so as to include the parent companies of utilities designated as investment-grade and as "distribution" utilities by S&P and further censored to include only those utilities with at least 50% of their revenues from utility operations.

4) See attached extract from S&P Report for the business profile scores attached in response to 2). Dr. Morin notes that S&P Business Risk scores only measure the business risk component of total investment risk and excludes financial risk. Moreover, business risk score examines risk from a bondholder viewpoint rather than from a shareholder viewpoint. The former is concerned mainly with ability to service debt and creditworthiness while the latter is concerned with variability and uncertainty of return.

5) Dr. Morin does not have access to that information. However, Dr. Morin does have the percentage of revenues from regulated electric operations for these companies. See attached AUS Utility Reports November 2007 edition

6) All else remaining constant (capital structure, size, regulatory risk, etc.), T&D operations are less risky than power generation. Dr. Morin notes that an electric utility with provider of last resort responsibility (POLR) can face a host of unique circumstances, ranging from a potential market redesign, customer base uncertainty, and supply uncertainty. All of these factors must be viewed against a recent backdrop of unprecedented electricity, gas, and emissions credit price volatility. Electric utilities with POLR responsibilities and witthout risk-mitigating policies are at least as risky as the typical vertically integrated electric utility and warrant similar returns and capital structures.

   Power generation activities are generally riskier than distribution operations, although there are exceptions. For example, distribution utilities with provider of last resort obligations in jurisdictions with retail choice, and/or distribution utilities located in high regulatory risk jurisdictions, and/or small-capitalization utilities, and/or utilities with weak balance sheets.

7) See answer to 5)

8) Generally higher.

9) On the whole, they are comparable in risk.

The use of parent company data to determine a utility subsidiary's cost of equity assumes that the subsidiary's risk and therefore its cost of equity is not substantially different from that of the parent company. Is the subsidiary's cost of common equity likely to change materially if it was not part of the parent company system? One can argue that as a large multi-unit company, the parent company enjoys greater diversification than its individual operating subsidiaries. In effect, risks are pooled, so the risk of the whole is less than the sum of the risks of the parts because of diversification. Moreover, holding companies may be able to operate on a more cost-effective basis by shifting energy resources in line with the relative supply-demand situation of the geographic areas of operation.

If the risk of all the subsidiaries in the consolidated parent company system are the same, the assumption that a given subsidiary's risk, and therefore its cost of equity, is similar to that of the consolidated parent is viable.

The parent company can be seen as a portfolio of companies, including both regulated companies and unregulated companies. From a conceptual viewpoint, on a stand-alone basis, the regulated companies are probably slightly less risky than the unregulated portions of the portfolio. But as a practical matter, if the regulated operations of the parent constitute the vast majority of the parent's activities and value, there is little distinction to be made between the subsidiary and the parent. If the risk-return properties of the parent portfolio are dominated by the risk-return properties of the regulated operations component, it is appropriate to assume that the parent derives its revenues predominantly from its regulated business, and is perceived by investors as a utility company.

As an additional practical matter, to the extent that equity investors in parent company stock are less than perfectly diversified, the parent's diversification activities actually reduce investor risk. Financial theory clearly states that portfolio diversification reduces risk for a given return if the components of the portfolio are less than perfectly correlated. As an added practical matter, the diversification activities of the parent may further reduce the utility's risk through a co-insurance effect stemming from its subsidiary activities. In short, if there is no quantifiable significant risk differential between the utility subsidiary and the parent, then their respective costs of debt and equity capital are virtually indistinguishable from one another. To the extent that the aforementioned co-insurance effect exists, and to the extent that corporate diversification benefits investors rather than homemade individual diversification, ratepayers benefit from a parent company's diversification efforts.

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ELECTRIC COMPANIES

	COMPANY	(1) LATEST 12 MONTHS EARNINGS AVAILABLE	(2) PER SHARE DATA ($) EARNINGS	(3) PER SHARE DATA ($) CURRENT ANNUAL DIVIDEND	(4) PER SHARE DATA ($) BOOK VALUE (1)	(5) PER SHARE DATA ($) STOCK PRICE 10/19/07	(6) COMMON SHARES O/S MILL	(7) PERCENT (2) DIV PAYOUT	(8) PERCENT (2) DIV YIELD	(9) PERCENT (2) MKT/ BOOK	(10) DIV/ BOOK (2)	(11) PRICE EARN MULT	(12)	(13)	(14) TOTAL REV $ MILL (1)	(15) REG ELEC REV	(16) NET PLANT $ MILL	(17) NET PLANT PER $ REV (1)	(18) S&P BOND RATING	(19) MOODY'S BOND RATING	(20) COMMON EQUITY RATIO (3)	(21) % RETURN ON BOOK VALUE COMMON EQUITY (4)	(22) % RETURN ON BOOK VALUE TOTAL CAPITAL	(23) REGULATION ALLOWED ROE	(24) REGULATION ORDER DATE	(25)
1	Allegheny Energy, Inc. (NYSE-AYE)	6/07	2.13	0.60	13.88	54.98	166.1	28	1.1	396	4.3	25.8			3,227.7	82	6,713.5	2.08	BBB+	Baa2	36	17.2	10.0	10.62	-	
2	ALLETE, Inc. (NYSE-ALE)	6/07	3.33	1.64	23.23	42.83	30.7	49	3.8	184	7.1	12.9			824.9	84	977.2	1.18	A-	Baa1	61	14.0	11.1	11.60	11/94	
3	American Electric Power Co. (NYSE-AEP)	6/07	2.44	1.56	24.19	45.63	399.2	64	3.4	189	6.4	18.7			12,940.0	92	28,467.0	2.20	BBB	Baa1	39	10.1	7.6	10.93	-	
4	Central Vermont Public Serv. Corp. (NYSE-CV)	6/07	1.83	0.92	17.67	31.26	10.2	50	2.9	177	5.2	17.1			328.6	100	313.9	0.96	BBB	NR	55	10.8	8.8	10.75	12/06	
5	Cleco Corporation (NYSE-CNL)	6/07	1.87	0.90	15.91	24.80	59.8	48	3.6	156	5.7	13.3			1,011.2	96	996.2	0.99	BBB+	Baa1	55	13.2	10.9	11.25	07/06	
6	DPL Inc.(NYSE-DPL)	6/07	1.36	1.04	6.88	26.05	113.6	76	4.0	379	15.1	19.2			1,466.2	100	2,686.3	1.83	BBB+	A3	33	20.8	10.4	11.00	12/05	
7	Edison International (NYSE-EIX)	6/07	3.47	1.16	24.66	54.16	325.8	33	2.1	220	4.7	15.6			12,829.0	80	16,544.0	1.29	A	A2	42	15.2	10.5	11.60	05/06	
8	El Paso Electric Company (ASE-EE)	6/07	1.31	0.00	13.11	22.56	45.7	0	0.0	172	NM	17.2			829.9	98	1,365.3	1.65	BBB	Baa2	50	10.4	8.5	11.25	-	
9	FirstEnergy Corporation (NYSE-FE)	6/07	4.27	2.00	28.34	65.51	304.8	47	3.1	231	7.1	15.3			12,163.0	88	15,010.0	1.23	BBB	Baa2	40	15.0	9.8	9.75	-	
10	FPL Group, Inc. (NYSE-FPL)	6/07	3.38	1.64	25.10	60.69	406.4	49	2.7	242	6.5	18.0			15,321.0	77	25,825.0	1.69	A	Aa3	44	14.0	9.4	11.75	08/05	
11	Great Plains Energy Incorporated (NYSE-GXP)	6/07	1.67	1.66	17.85	29.02	85.6	99	5.7	163	9.3	17.4			2,943.0	40	3,204.0	1.09	BBB	A2	52	9.7	7.9	-	-	
12	Hawaiian Electric Industries, Inc. (NYSE-HE)	6/07	0.89	1.24	13.53	22.07	81.9	139	5.6	163	9.2	24.8			2,435.8	83	2,938.1	1.21	BBB	Baa2	26	6.3	3.6	10.82	-	
13	IDACORP, Inc. (NYSE-IDA)	6/07	2.16	1.20	26.40	32.76	44.3	56	3.7	124	4.5	15.2			835.8	99	2,473.2	2.96	A	A3	48	8.4	6.8	-	-	
14	Maine & Maritimes Corporation (ASE-MAM)	6/07	-0.36	0.00	25.62	29.45	1.7	0	0.0	115	NM	NM			33.5	96	60.4	1.80	NR	NR	53	NM	NM	10.20	07/06	
15	OGE Energy Corp. (NYSE-OGE)	6/07	2.43	1.36	17.45	34.49	92.7	56	3.9	198	7.8	14.2			3,786.4	45	4,023.3	1.06	BBB +	Baa2	55	14.6	11.1	10.38	-	
16	Otter Tail Corporation (NDQ-OTTR)	6/07	1.69	1.17	16.97	34.27	29.9	69	3.4	202	6.9	20.3			1,174.2	26	763.7	0.65	BBB+	A3	58	10.3	8.4	12.00	-	
17	Pinnacle West Capital Corp. (NYSE-PNW)	6/07	2.88	2.10	34.19	40.63	100.1	73	5.2	119	6.1	14.1			3,365.1	80	8,118.0	2.41	BBB-	Baa2	50	8.6	7.5	10.75	06/28	
18	Portland General Electric (NYSE-POR)	6/07	2.42	0.94	38.46	26.97	62.5	39	3.5	70	2.4	11.1			1,626.0	99	2,892.0	1.78	BBB+	Baa1	64	6.6	6.3	10.80	1/07	
19	Progress Energy Inc. (NYSE-PGN)	6/07	2.86	2.44	31.81	45.12	259.0	85	5.4	142	7.7	15.8			9,926.0	89	15,751.0	1.59	A-	A2	46	9.0	7.2	12.42	-	
20	Southern Company (NYSE-SO)	6/07	2.26	1.61	15.57	35.40	757.0	71	4.5	227	10.3	15.7			14,882.4	98	29,189.9	1.96	A	A1	41	15.0	9.6	12.20	-	
21	UIL Holdings Corporation (NYSE-UIL)	6/07	1.86	1.73	17.93	31.10	25.3	93	5.6	173	9.6	16.7			937.2	100	717.6	0.77	NR	Baa2	46	9.8	7.2	9.75	01/06	
22	Westar Energy, Inc. (NYSE-WR)	6/07	1.80	1.08	18.24	24.71	90.7	60	NM	135	5.9	13.7			1,644.6	73	4,397.8	2.67	BBB-	Baa2	45	10.6	8.2	10.00	12/05	
	AVERAGE							58	3.5	190	7.1	16.8									47	11.9	8.6	10.99		

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COMBINATION ELECTRIC & GAS COMPANIES

	COMPANY	LATEST 12 MONTHS EARNINGS AVAILABLE	PER SHARE DATA ($) EARNINGS	CURRENT ANNUAL DIVIDEND	BOOK VALUE (1)	STOCK PRICE 10/19/07	COMMON SHARES O/S MILL	PERCENT (2) DIV PAYOUT	DIV YIELD	MKT/ BOOK	DIV/ BOOK (2)	PRICE EARN MULT	TOTAL REV $ MILL (1)	REG ELEC REV	NET PLANT $ MILL	NET PLANT PER $ REV (1)	S&P BOND RATING	MOODY'S BOND RATING	COMMON EQUITY RATIO (3)	% RETURN ON BOOK VALUE COMMON EQUITY (4)	TOTAL CAPITAL	REGULATION ALLOWED ROE	ORDER DATE
1	Alliant Energy Corporation (NYSE-LNT)	6/07	3.36	1.27	22.09	37.82	113.0	38	3.4	171	5.8	11.3	3,390.6	71	4,699.2	1.39	A-	A2	51	15.6	11.2	11.02	-
2	Ameren Corporation (NYSE-AEE)	6/07	3.00	2.54	31.97	52.46	207.0	85	4.8	164	7.9	17.5	7,272.0	82	14,538.0	2.00	BBB-	Baa2	47	9.6	7.9	10.37	-
3	Aquila Inc. (NYSE-ILA)	6/07	-0.14	0.00	3.44	4.04	374.8	0	0.0	117	NM	NM	1,398.4	56	1,870.3	1.34	B+	Ba3	55	NM	3.9	10.51	-
4	Avista Corporation (NYSE-AVA)	6/07	1.08	0.60	17.54	20.22	52.8	56	3.0	115	3.4	18.7	1,482.9	48	2,267.6	1.53	BBB-	Baa3	46	6.5	7.6	10.40	-
5	Black Hills Corporation (NYSE-BKH)	6/07	2.85	1.36	25.71	41.29	37.7	48	3.3	161	5.3	14.5	681.7	28	1,747.9	2.56	BBB	Baa1	57	11.7	9.2	-	-
6	CenterPoint Energy (NYSE-CNP)	6/07	1.54	0.68	5.25	15.97	321.2	44	4.3	304	13.0	10.4	9,538.0	19	9,549.0	1.00	BBB	Baa2	15	23.5	8.5	10.14	10/06
7	CH Energy Group, Inc. (NYSE-CHG)	6/07	3.02	2.16	33.22	44.96	15.8	72	4.8	135	6.5	14.9	1,076.7	52	850.7	0.79	A	A2	55	9.2	7.5	9.60	7/06
8	CMS Energy Corporation (NYSE-CMS)	6/07	-0.63	0.20	6.29	16.06	350.0	NM	1.2	255	3.2	NM	6,957.0	50	7,820.0	1.12	BBB	Baa1	24	NM	2.1	11.08	-
9	Consolidated Edison, Inc. (NYSE-ED)	6/07	3.27	2.32	33.08	45.12	266.2	71	5.1	136	7.0	13.8	12,711.0	62	18,290.0	1.44	A	A1	50	10.4	8.4	10.53	-
10	Constellation Energy Group, Inc. (NYSE-CEG)	6/07	4.97	1.74	28.63	88.07	180.2	35	2.0	308	6.1	17.7	19,902.6	11	9,526.6	0.48	A	Baa1	50	19.3	12.6	11.00	-
11	Dominion Resources, Inc. (NYSE-D)	6/07	2.65	2.84	36.04	85.99	349.0	107	3.3	239	7.9	32.4	16,442.0	34	29,504.0	1.79	BBB+	Baa2	39	5.8	6.3	10.50	-
12	DTE Energy Company (NYSE-DTE)	6/07	4.83	2.12	34.51	47.53	170.6	44	4.5	138	6.1	9.8	9,176.0	52	11,460.0	1.25	BBB+	A3	41	14.7	7.8	11.00	-
13	Duke Energy Corporation (NYSE-DUK)	6/07	1.39	0.88	16.21	18.41	1260.0	63	4.8	114	5.4	13.2	14,374.0	59	29,799.0	2.07	A	A3	63	7.7	6.9	11.18	-
14	Empire District Electric Co. (NYSE-EDE)	6/07	1.42	1.28	15.45	22.48	30.3	90	5.7	145	8.3	15.8	471.6	86	1,098.8	2.33	BBB+	Baa1	44	8.8	7.1	10.90	-
15	Energy East Corporation (NYSE-EAS)	6/07	1.69	1.20	20.35	27.40	158.1	71	4.4	135	5.9	16.2	5,224.1	57	5,871.0	1.12	A-	A3	45	8.3	7.8	10.69	-
16	Entergy Corporation (NYSE-ETR)	6/07	5.50	3.00	39.72	112.19	196.1	55	2.7	282	7.6	20.4	11,105.2	82	20,834.5	1.88	BBB+	Baa2	41	14.4	9.8	10.81	-
17	Exelon Corporation (NYSE-EXC)	6/07	2.98	1.76	16.57	75.14	674.2	59	2.3	453	10.6	25.2	17,426.0	60	23,431.0	1.34	BBB+	A3	46	18.5	11.7	10.05	-
18	Florida Public Utilities Company (ASE-FPU)	6/07	0.57	0.45	8.09	11.94	6.0	79	3.8	148	5.6	20.9	132.2	39	132.0	1.00	NR	Aaa	48	7.0	7.5	11.28	-
19	Integrys Energy Group (NYSE-TEG)	6/07	2.67	2.64	41.82	51.44	75.9	99	5.1	123	6.3	19.3	8,482.0	14	4,325.0	0.51	A	A1	50	5.5	5.6	11.21	-
20	MDU Resources Group, Inc. (NYSE-MDU)	6/07	1.74	0.58	12.41	27.46	181.8	33	2.1	221	4.7	15.8	4,052.6	5	3,101.3	0.77	BBB+	A2	62	14.7	11.0	11.83	-
21	MGE Energy, Inc. (NDQ-MGEE)	6/07	2.22	1.42	19.11	33.05	21.4	64	4.3	173	7.4	14.9	527.7	62	760.7	1.44	AA	Aa2	58	12.1	8.9	11.00	01/06
22	NiSource Inc. (NYSE-NI)	6/07	1.30	0.92	18.46	19.64	274.9	71	4.7	106	5.0	15.1	7,676.9	18	9,462.9	1.23	BBB	Baa2	45	7.3	6.8	11.33	-
23	Northeast Utilities (NYSE-NU)	6/07	1.67	0.80	18.19	27.98	155.2	48	2.9	154	4.4	16.8	6,173.6	84	6,645.5	1.08	BBB	Baa1	45	9.8	10.2	9.86	-
24	Northwestern Corporation (NYSE-NWEC)	6/07	1.08	1.32	21.02	27.18	36.0	122	4.9	129	6.3	25.2	1,165.2	59	1,586.9	1.36	BBB-	Baa3	52	5.5	6.6	11.46	-
25	NSTAR (NYSE-NST)	6/07	2.02	1.30	15.44	33.82	106.8	64	3.8	219	8.4	16.7	3,467.9	80	4,029.6	1.16	A+	A1	36	13.5	8.6	12.50	12/05
26	Pepco Holdings, Inc. (NYSE-POM)	6/07	1.31	1.04	13.86	26.54	193.2	79	3.9	192	7.5	20.3	8,757.5	51	7,651.6	0.87	BBB+	Baa1	35	8.0	7.0	10.15	-
27	PG&E Corporation (NYSE-PCG)	6/07	2.93	1.44	23.42	45.70	350.0	49	3.2	195	6.1	15.6	12,917.0	71	22,542.0	1.75	BBB+	Baa1	43	13.7	9.9	11.35	3/07
28	PNM Resources, Inc. (NYSE-PNM)	6/07	1.75	0.92	22.50	23.62	76.7	53	3.9	105	4.1	13.5	2,503.4	79	3,303.9	1.32	BBB	Baa2	43	8.5	7.0	10.13	-
29	PPL Corporation (NYSE-PPL)	6/07	2.19	1.22	13.95	47.62	385.0	56	2.6	341	8.7	21.7	6,727.0	66	11,982.0	1.78	A-	A3	40	16.6	10.5	9.57	-
30	Public Service Enterprise Group (NYSE-PEG)	6/07	4.64	2.34	26.95	88.38	254.0	50	2.6	328	8.7	19.0	12,650.0	63	13,279.0	1.05	A-	A3	38	17.6	11.0	9.88	-
31	Puget Energy, Inc. (NYSE-PSD)	6/07	1.64	1.00	18.60	23.75	117.2	61	4.2	128	5.4	14.5	3,118.8	61	5,426.6	1.74	BBB+	Baa2	42	8.9	7.7	10.40	02/05
32	SCANA Corporation (NYSE-SCG)	6/07	2.53	1.76	24.81	39.27	116.7	70	4.5	158	7.1	15.5	4,600.0	42	7,179.0	1.56	A-	A1	44	10.2	7.8	10.71	-
33	SEMPRA Energy (NYSE-SRE)	6/07	4.52	1.24	30.15	58.16	265.0	27	2.1	193	4.1	12.9	11,604.0	41	14,050.0	1.21	A+	A1	61	15.9	12.2	10.70	-
34	Sierra Pacific Resources (NYSE-SRP)	6/07	1.36	0.32	12.08	15.14	221.3	24	2.1	125	2.6	11.1	3,435.3	94	5,794.1	1.69	BB+	Ba1	38	12.2	8.9	10.48	-
35	TECO Energy, Inc. (NYSE-TE)	6/07	1.24	0.78	8.65	15.85	210.0	63	4.9	183	9.0	12.8	3,436.9	61	4,755.8	1.38	BBB-	Baa2	33	15.0	9.8	11.25	-
36	UniSource Energy Corporation (NYSE-UNS)	6/07	1.51	0.90	18.51	30.60	35.4	60	2.9	165	4.9	20.3	1,341.1	85	2,313.2	1.72	BBB	Baa2	34	8.8	10.6	10.67	-
37	Unitil Corporation (ASE-UTL)	6/07	1.56	1.38	17.09	28.93	5.7	88	4.8	169	8.1	18.5	266.7	86	243.8	0.91	NR	NR	34	9.2	7.3	9.84	1/07
38	Vectren Corporation (NYSE-VVC)	6/07	1.75	1.26	15.89	26.87	76.7	72	4.7	169	7.9	15.4	2,205.3	20	2,449.6	1.11	A	A3	44	11.3	8.4	10.53	-
39	Wisconsin Energy Corporation (NYSE-WEC)	6/07	2.35	1.00	25.14	44.82	118.5	43	2.2	178	4.0	19.1	4,142.6	63	7,486.6	1.81	A-	Aa3	40	10.6	6.7	11.20	01/06
40	Xcel Energy Inc. (NYSE-XEL)	6/07	1.33	0.92	14.29	21.02	419.5	69	NM	147	6.4	15.8	9,909.3	78	16,109.7	1.63	A-	A3	44	9.7	8.0	10.83	-
	AVERAGE							60	3.5	192	6.5	16.9							44	11.2	8.4	10.72	
	COMBINED ELECTRIC/COMBINATION ELECTRIC & GAS AVERAGES							59	3.5	191	6.7	16.9							45	11.5	8.4	10.81	

LATEST ISSUE - AUS MONTHLY REPORT

November 2007

COMPOSITE INDEX

ELECTRIC COMPANIES

		DIVIDEND YIELD	PRICE EARNINGS MULTIPLE
YEAR	1997	6.1	13.3
YEAR	1998	4.8	16.6
YEAR	1999	4.8	15.2
YEAR	2000	5.4	13.6
YEAR	2001	4.5	14.0
YEAR	2002	5.0	14.8
YEAR	2003	5.0	15.4
YEAR	2004	4.4	18.4
YEAR	2005	4.1	20.9
YEAR	2006	3.8	20.8
YEAR TO DATE	2007	3.4	18.6
DECEMBER	2006	3.4	20.0
JANUARY	2007	3.3	18.8
FEBRUARY	2007	3.4	18.7
MARCH	2007	3.3	19.5
APRIL	2007	3.4	19.0
MAY	2007	3.2	19.9
JUNE	2007	3.2	20.7
JULY	2007	3.5	18.9
AUGUST	2007	3.4	18.7
SEPTEMBER	2007	3.4	16.0
OCTOBER	2007	3.5	17.1
NOVEMBER	2007	3.5	16.8

COMBINATION GAS & ELECTRIC COMPANIES

		DIVIDEND YIELD	PRICE EARNINGS MULTIPLE
YEAR	1997	6.0	13.6
YEAR	1998	4.8	16.7
YEAR	1999	4.7	16.0
YEAR	2000	5.0	16.1
YEAR	2001	4.1	15.3
YEAR	2002	4.9	14.9
YEAR	2003	3.8	15.3
YEAR	2004	3.4	17.1
YEAR	2005	3.3	18.9
YEAR	2006	3.2	18.7
YEAR TO DATE	2007	3.3	18.3
DECEMBER	2006	3.2	18.7
JANUARY	2007	3.2	18.8
FEBRUARY	2007	3.3	18.8
MARCH	2007	3.2	19.8
APRIL	2007	3.3	18.6
MAY	2007	3.1	19.8
JUNE	2007	3.1	19.5
JULY	2007	3.3	19.0
AUGUST	2007	3.4	17.5
SEPTEMBER	2007	3.5	16.5
OCTOBER	2007	3.6	16.6
NOVEMBER	2007	3.5	16.9

NATURAL GAS DISTRIBUTION COMPANIES

		DIVIDEND YIELD	PRICE EARNINGS MULTIPLE
YEAR	1997	4.7	15.2
YEAR	1998	4.3	17.9
YEAR	1999	4.4	19.5
YEAR	2000	4.3	19.0
YEAR	2001	4.1	16.6
YEAR	2002	4.3	17.3
YEAR	2003	4.0	16.2
YEAR	2004	3.3	17.0
YEAR	2005	3.1	19.8
YEAR	2006	3.1	17.2
YEAR TO DATE	2007	2.9	19.6
DECEMBER	2006	2.9	19.4
JANUARY	2007	2.9	19.5
FEBRUARY	2007	3.0	19.2
MARCH	2007	2.9	19.9
APRIL	2007	2.9	19.8
MAY	2007	2.8	21.2
JUNE	2007	2.7	21.2
JULY	2007	2.7	21.1
AUGUST	2007	2.8	20.1
SEPTEMBER	2007	2.9	17.9
OCTOBER	2007	2.9	17.7
NOVEMBER	2007	2.9	18.3

TELEPHONE COMPANIES

		DIVIDEND YIELD	PRICE EARNINGS MULTIPLE
YEAR	1997	3.0	17.6
YEAR	1998	2.0	24.4
YEAR	1999	1.5	28.2
YEAR	2000	0.9	27.9
YEAR	2001	0.9	26.3
YEAR	2002	1.4	21.1
YEAR	2003	1.7	21.6
YEAR	2004	2.3	21.5
YEAR	2005	2.6	22.5
YEAR	2006	2.6	21.1
YEAR TO DATE	2007	2.7	20.4
DECEMBER	2006	2.4	19.6
JANUARY	2007	2.4	19.1
FEBRUARY	2007	2.6	17.6
MARCH	2007	2.5	18.2
APRIL	2007	3.1	19.0
MAY	2007	2.7	21.7
JUNE	2007	2.7	20.6
JULY	2007	2.6	20.6
AUGUST	2007	2.7	20.7
SEPTEMBER	2007	2.9	22.4
OCTOBER	2007	2.9	22.0
NOVEMBER	2007	2.8	22.3

SMALL TELEPHONE COMPANIES

		DIVIDEND YIELD	PRICE EARNINGS MULTIPLE
YEAR	1997	NA	NA
YEAR	1998	NA	NA
YEAR	1999	NA	NA
YEAR	2000	2.4	24.4
YEAR	2001	2.8	20.0
YEAR	2002	2.6	20.1
YEAR	2003	2.8	21.7
YEAR	2004	2.6	19.3
YEAR	2005	3.5	17.2
YEAR	2006	3.8	21.6
YEAR TO DATE	2007	4.4	20.8
DECEMBER	2006	3.8	21.6
JANUARY	2007	3.8	22.2
FEBRUARY	2007	4.3	21.9
MARCH	2007	4.3	22.0
APRIL	2007	4.4	20.9
MAY	2007	4.4	23.7
JUNE	2007	4.7	24.9
JULY	2007	4.2	21.2
AUGUST	2007	4.2	21.2
SEPTEMBER	2007	4.4	19.0
OCTOBER	2007	4.6	14.6
NOVEMBER	2007	4.9	17.0

WATER COMPANIES

		DIVIDEND YIELD	PRICE EARNINGS MULTIPLE
YEAR	1997	5.2	15.1
YEAR	1998	4.4	17.2
YEAR	1999	3.7	19.7
YEAR	2000	3.5	21.4
YEAR	2001	3.4	21.4
YEAR	2002	3.1	22.2
YEAR	2003	3.2	23.2
YEAR	2004	3.1	27.9
YEAR	2005	2.8	28.7
YEAR	2006	2.8	30.9
YEAR TO DATE	2007	2.8	28.0
DECEMBER	2006	2.8	33.0
JANUARY	2007	2.9	27.0
FEBRUARY	2007	2.9	26.8
MARCH	2007	2.8	27.6
APRIL	2007	2.9	25.5
MAY	2007	2.8	26.4
JUNE	2007	2.9	27.0
JULY	2007	2.9	26.6
AUGUST	2007	2.8	32.0
SEPTEMBER	2007	2.8	29.4
OCTOBER	2007	2.7	30.1
NOVEMBER	2007	2.9	30.1

State of New York
Department of Public Service

Orange & Rockland Utilities, Inc.
Case No. 07-E-0949

Information/Document Request

Request No.:	DPS-97
Requested By:	Michael J. Augstell (518) 486-2874
Date of Request:	11/01/07
Reply Date:	11/11/07
Witness:	Roger A. Morin
Subject:	Cost of Equity Methodology

(1) For the CAPM and the Empirical CAPM risk premium analyses Dr. Morin performed, did he consider historical studies of long-term risk premiums other than the Ibbotson Associates study, Stocks, Bonds, Bills and Inflation: Valuation Edition, 2007 Yearbook? If so, which ones?

(2) For the CAPM and the Empirical CAPM risk premium analyses Dr. Morin performed, did he consider forward looking studies of long-term risk premiums other than that calculated by using Value Line's VLIA software or the research by Harris, Marston, Mishra and O'Brien? If so, which ones?

Response:

1) Yes. In the latest edition of Ibbotson Associates' (now Morningstar) widely-used Valuation Yearbook, 2007 edition, Ibbotson and Chen have updated their study of the prospective MRP and conclude:

> *"Contrary to several recent studies on equity risk premium that declare the forward-looking equity risk premium to be close to zero, or even negative, Ibbotson and Chen have found the long-term supply of equity risk premium to be only slightly lower than the straight historical estimate."*

In other words, prospective estimates of the MRP are virtually the same as the historical MRP.

Professor Siegel[1] from the Wharton School of Finance has also examined historical data over even longer time series, including data prior to 1926, some dating back to 1802. An obvious question is whether data on capital market behavior from the 19th century relevant for estimating return in the 21st century. The major concern with the Siegel data for a period beginning in 1802 is the reliability of the data. The stock market of the early 1800's was severely limited, embryonic in scope, with very few issues trading, and few industries represented. Dividend data were unavailable over most of this early period and stock prices were based on wide bid-ask spreads rather than on actual transaction prices. The difficulties inherent in stock market data prior to the Great Depression are discussed by Schwert.[2]

Published work by Dimson, Marsh, and Staunton[3] report historical returns over the period 1900 to 2000 for twelve countries, representing 90% of today's world market capitalization. They report an average risk premium over long bond returns over all countries of 5.6%, with the U.S. at 7.0%. The premium was generally higher for the second half century than for the first. For example, the U.S. had 5% in the first half, compared to 7.5% in the second half.

2) Dr. Morin is well aware of the state of research on the market risk premium (MRP). The academic research on the MRP is vast and often contradictory.

Dr. Morin's estimate of the prospective MRP is quite consistent with the gist of the literature on the subject. Chapter 5 of Dr. Morin's book The New Regulatory Finance provides a comprehensive summary of that literature. To highlight some of the more salient passages, Ibbotson's (now Morningstar) *Stocks, Bonds, Bills, and Inflation 2007 Yearbook* finds that a broad market sample of U.S. common stocks outperformed long-term U.S. government bonds by 6.5 percent. The historical MRP over the income component of long-term Treasury bonds rather than over the total return is 7.1 percent. It has been common practice to assume that this historical result provides an adequate basis for the expected MRP.

In their widely-used textbook, Brealey, Myers, and Allen state: "We have no official position on the exact market risk premium, but we believe a range of 6 to 8 percent is reasonable for the United States."[4]

Published work by Dimson, Marsh, and Staunton[5] reports returns over the period 1900 to 2000 for twelve countries, representing 90% of today's world market capitalization.

[1] Siegel, Jeremy (1999) "The shrinking equity premium." Journal of Portfolio Management 26(1): 10-17.

[2] Schwert, G. W., "Indexes of U.S. Stock Prices from 1802 to 1987," Journal of Business, 1990, Vol. 63, no. 3.

[3] Dimson, Elroy, Paul Marsh and Mike Staunton (2000) "Risk and Return in the 20th and 21st centuries." Business Strategy Review 11(2): 1-18.

[4] Brealey, R.,Myers, S., and Allen, P., *Principles of Corporate Finance,* 8th ed. New York: McGraw-Hill, 2006.

They report an average risk premium over long bond returns over all countries of 5.6 percent, with the United States at 7.0 percent. The premium was generally higher for the second half century than for the first. For example, the U.S. had 5 percent in the first half, compared to 7.5 percent in the second half.

A second approach to estimating the MRP is prospective in nature and consists of applying the DCF model to an aggregate equity index, as Dr. Morin did in his direct testimony.

A prospective study cited in direct testimony and published in *Financial Management* by Harris, Marston, Mishra, and O'Brien ("HMMO") provides estimates of the ex ante expected returns for S&P 500 companies over the period 1983-1998.[6] From that study, the average MRP estimate for the overall period is 7.2 percent.

In terms of the most recent credible research on the issue, in the latest edition of Ibbotson Associates' (now Morningstar) widely-used Valuation Yearbook, 2007 edition, Ibbotson and Chen have updated their study of the prospective MRP and conclude:

> *"Contrary to several recent studies on equity risk premium that declare the forward-looking equity risk premium to be close to zero, or even negative, Ibbotson and Chen have found the long-term supply of equity risk premium to be only slightly lower than the straight historical estimate."*

In other words, prospective estimates of the MRP are comparable to historical estimates.

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[5] Dimson, Elroy, Paul Marsh and Mike Staunton (2000) "Risk and Return in the 20th and 21st centuries." *Business Strategy Review* 11(2): 1-18.

[6] Harris, R. S., Marston, F. C., Mishra, D. R., and O'Brien, King. J., "*Ex Ante* Cost of Equity Estimates of S&P 500 Firms: The Choice Between Global and Domestic CAPM," *Financial Management*, Autumn 2003, pp. 51-66.