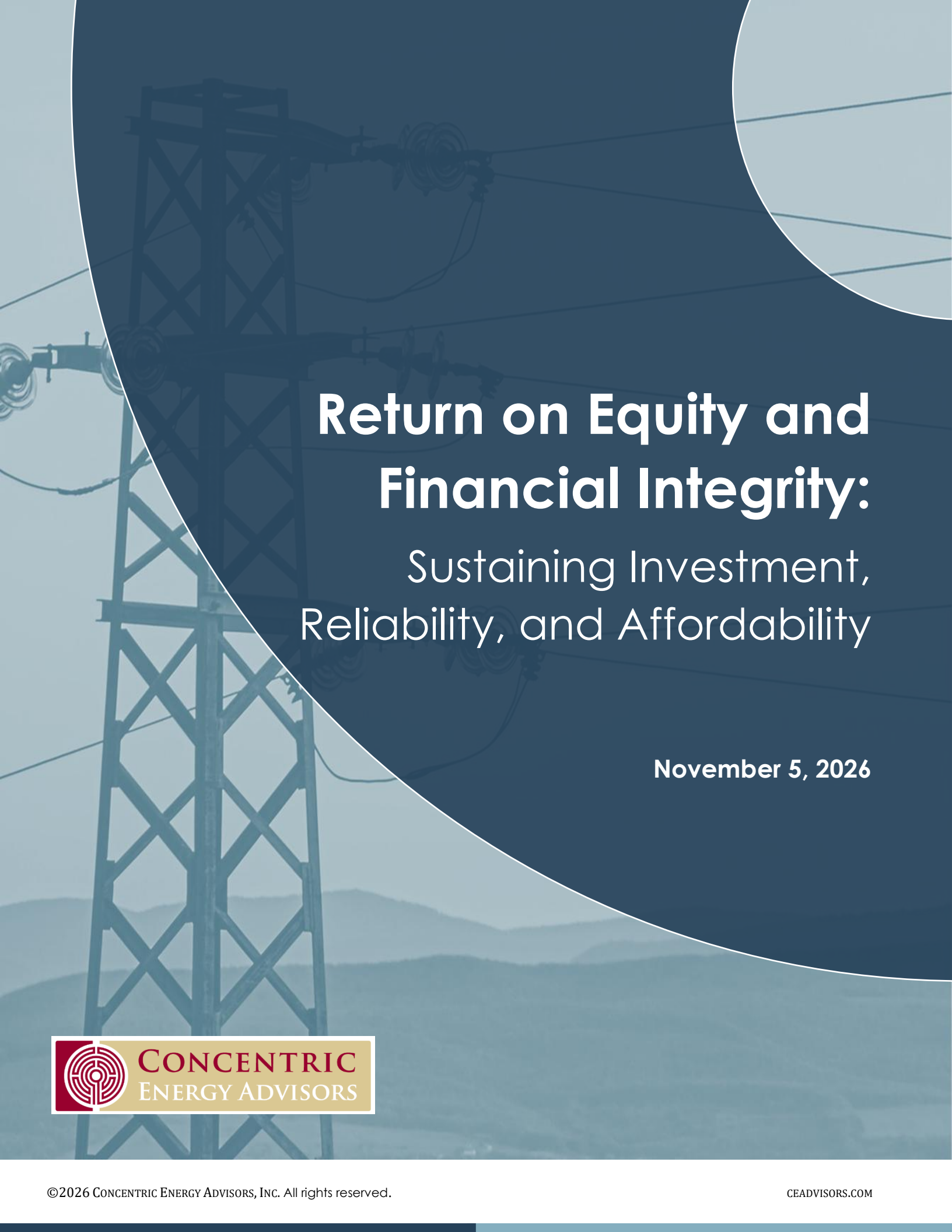


Return on Equity and Financial Integrity:

Sustaining Investment, Reliability, and Affordability

November 5, 2026

CONCENTRIC ENERGY ADVISORS

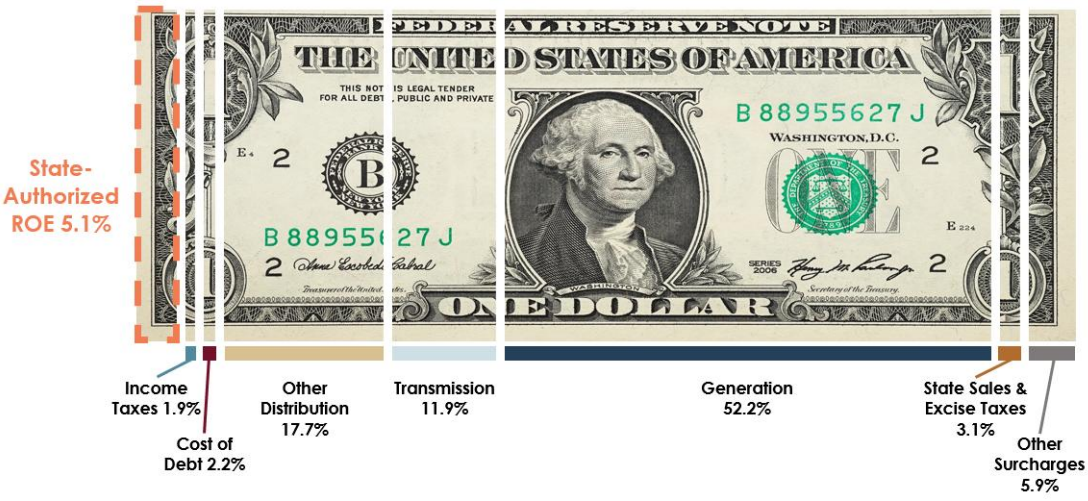
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This paper examines the role of return on equity (ROE) in utility regulation and, in particular, the relationship between authorized ROEs, customer bills and the cost of providing service, and utilities' ability to attract the capital needed to provide safe and reliable service.

The U.S. regulatory model has enabled electric utilities to finance exceptionally capital-intensive infrastructure with reasonably priced investor capital while protecting customers through comprehensive regulatory oversight. That structure is increasingly important as utilities undertake a major cycle of investment to meet growing electricity demand, strengthen reliability and resilience, connect new customers, and replace aging infrastructure. Maintaining utilities' ability to attract capital on reasonable terms will help ensure that this investment can be made efficiently and at the lowest reasonable long-term cost to customers. This paper reaches four principal conclusions:

1. **Outside investment is critical for regulated investor-owned utilities to meet essential public needs.** For more than a century, the regulatory compact has required utilities to serve all customers and submit their investments, rates, and operations to regulatory oversight in exchange for a reasonable opportunity to recover prudently incurred costs and earn a fair return on invested capital. Under this system, state regulators, not utilities, ultimately determine the rates that customers pay. That framework is especially valuable now to finance and build necessary infrastructure.
2. **ROE represents a relatively small component of the customer bill and should be considered in the context of the broader cost of providing electric service.** Across the paper's national and regional analyses, the equity return associated with state-authorized ROE on distribution assets generally represents approximately 5 percent of the total electric bill, depending on the region, with the national analysis producing mean and median estimates of 4.3 to 5.1 percent. Authorized ROEs also have declined over the long term and, in recent years, have not increased commensurately with higher borrowing costs.

Figure ES-1. Components of a Typical Residential Electric Bill in PJM[1]

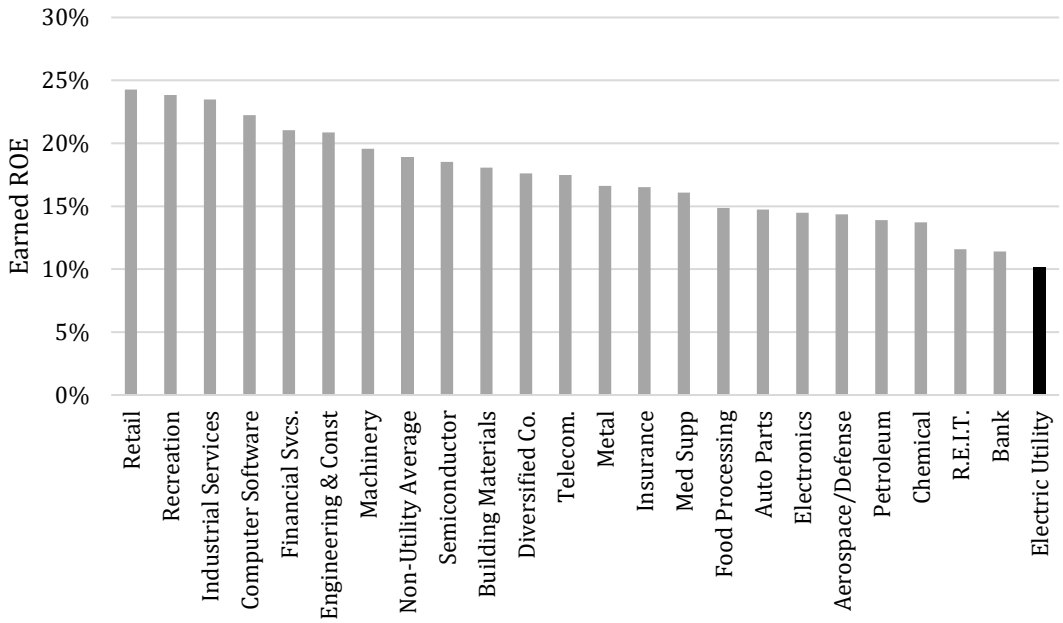


[1] State-Authorized ROE includes the equity return authorized by a state utility commission. Income Taxes includes distribution-related federal and state income taxes and the Ohio Commercial Activity Tax. Cost of Debt includes distribution-related interest on utility debt. Other Distribution includes all other costs recovered through distribution rates and distribution infrastructure riders, such as operations and maintenance expense, depreciation, and property taxes. Transmission includes retail transmission charges, which recover transmission costs including ROE that are set under FERC-regulated rates. Generation includes energy and capacity supply, calculated using default service generation rates. State Sales & Excise Taxes includes state sales, excise, and similar taxes on electricity sales and use. Other Surcharges includes other riders, such as energy efficiency, universal service, and clean energy programs.

Policymakers seeking meaningful affordability improvements should therefore focus primarily on larger and faster-growing cost drivers outside of utilities' control, including wholesale electricity prices, capacity costs, and policy and compliance costs. Figure ES-1 shows the components of a typical residential electric utility bill based on a sample of utilities in the PJM region as an example.

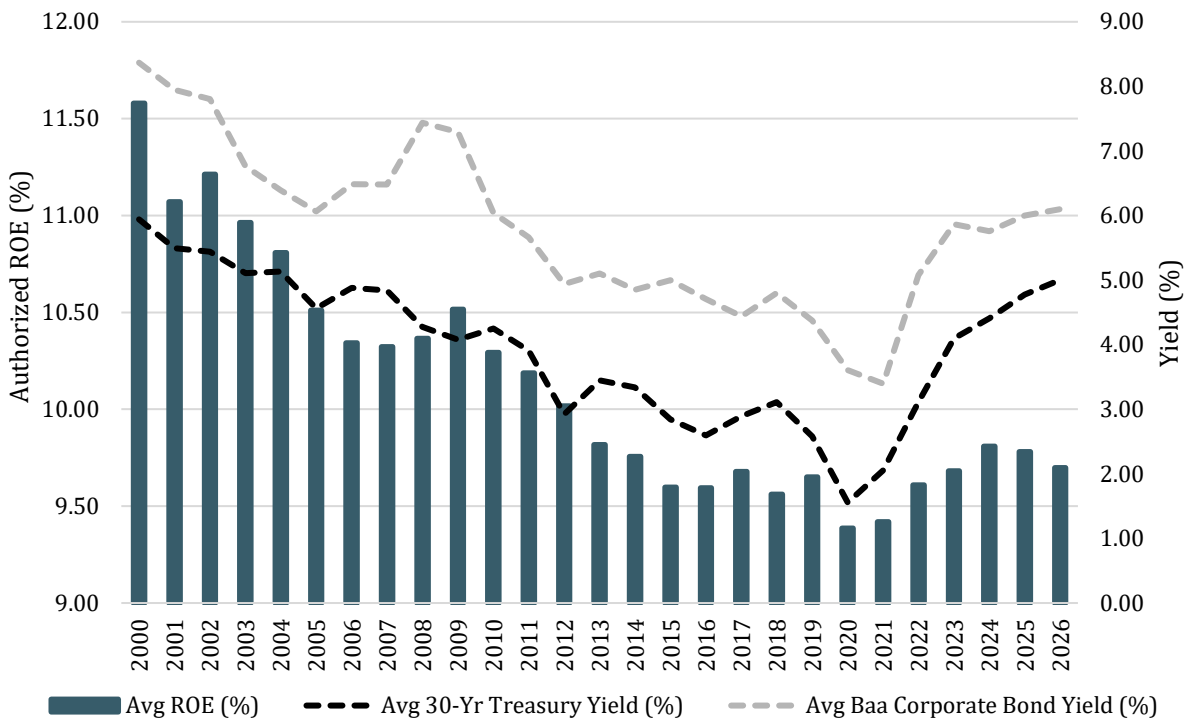
3. **Utility returns on equity are among the lowest compared to other industries (see Figure ES-2).** An authorized ROE is not a specified profit margin, nor is it a guaranteed profit. Rather, it represents an opportunity to earn a return if utility management operates the business efficiently, investment decisions are prudent, and regulators ultimately allow the utility to recover its costs through rates. Electric utilities' actual earned returns and total shareholder returns are comparatively modest, even as utilities are nearly three times as capital intensive as the typical non-utility company and must repeatedly access external capital because their investment needs exceed internally generated cash. The premium of authorized ROEs over corporate borrowing costs has also narrowed in recent years as authorized ROEs lagged market indicators that point to increases in the cost of capital (see Figure ES-3). In addition, actual earned returns are often lower than the authorized level.

Figure ES-2. Average Earned ROEs – Electric Utilities vs. Other Sectors



4. **Regulated utilities' ability to attract investor capital is critical for lower customer rates.** Utilities have historically leveraged the regulated utility model to access relatively low-cost capital compared to other industries and other sectors of the energy industry. That lower cost of capital is beneficial to customers and has enabled utilities to provide electricity at prices that have increased at a rate lower than general inflation in recent decades. In other words, on an inflation adjusted basis, electricity prices in real terms have declined since 1990. This benefit to customers can only be sustained by maintaining a strong financial position. In contrast, the case studies presented in this paper show how weakened financial integrity, which can result from an insufficient ROE, can lead to credit downgrades, higher borrowing costs, constrained capital access, and deferred or reallocated investment. Because utility debt is often issued for 10, 20, or 30 years, higher financing costs can remain embedded in customer rates long after the conditions that produced them have changed. Preserving financial integrity helps utilities retain financial flexibility and fund necessary investment through changing economic conditions while maintaining safe, reliable, and affordable service.

Figure ES-3. Authorized Electric ROEs vs. 30-Year Treasury and Baa Corporate Bond Yields



Proposals to impose materially lower ROEs without clear evidence that capital costs have declined or the utility's total risk has fallen, to substitute untested methodologies, or to require utilities to finance operations with substantially more debt overlook the resulting financial risk: reduced ROEs and greater leverage can weaken credit metrics and increase both debt and equity costs, offsetting anticipated savings and ultimately raising risks and costs for customers.

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