



# TransRiskPricing

## TranRiskPricing© Provides Analytical Solutions to FERC Transmission Pricing Incentive

TranRiskPricing© provides a comprehensive solution for transmission investment analysis by incorporating multiple risk factors beyond existing infrastructure costs into pricing. This mitigates regulatory and operational risks and increases financial returns. This innovative model applies cutting edge investment concepts to leverage the new FERC Transmission Pricing Incentive Ruling, and it calculates both risk-based incentive components of pricing and the existing infrastructure cost.



## TranRiskPricing© Estimates Base-case Scenario for Rate Structure

The model captures the current FERC transmission tariff filing including the following infrastructure cost parameters:

- ✦ Cost Allocators and Plant Calculation
- ✦ Operations and Maintenance
- ✦ Depreciation, Amortization and Tax Expense
- ✦ Capitalization and other Revenue Requirements

## TranRiskPricing© Overlays Strategic Business Structures

Emerging transmission investment structures represent drastic changes in corporate risk profiles. Each structure impacts the various investment risk factors. Emerging structures considered include:

- ✦ Subsidiary or Affiliate of Investor-owned Utility
  - Form Transmission Company LLC under parent company
  - Expand the existing asset territory to “Outside of the Fence”
  - Acquire transmission company assets, and then build merchant transmission lines “Inside of the Fence”
- ✦ Independent Transmission Company
- ✦ Joint venture with Transmission Owners in ISO-controlled area
- ✦ Joint venture with IOUs in IOU-controlled area
- ✦ Public/Private Partnership via DOE/State Alliance

## TranRiskPricing© Incorporates Key Investment Risk Factors

Risks and returns depend on the structure of new transmission investments, the method of revenue collection, and the ability to absorb loss exposure on the balance sheet.

Key investment risk factors include:

- ✦ Regulatory uncertainties causing business risks
- ✦ General market risks
- ✦ Capital market risk
- ✦ Enterprise credit risk
- ✦ Operational risk
- ✦ Legal and liability risk
- ✦ Critical resource issues

### Contact

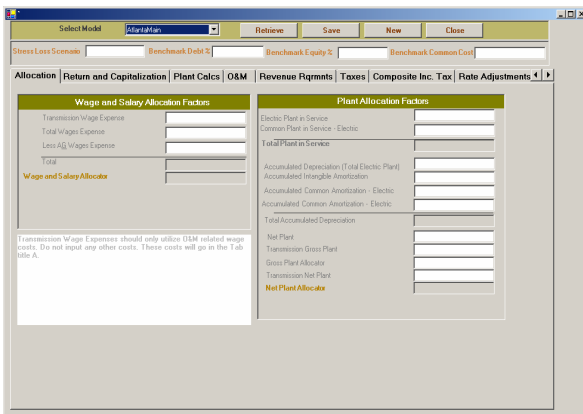
Jenny Hou	202-262-9933	<a href="mailto:info@jh2risk.com">info@jh2risk.com</a>
Frank Lin	917-941-4161	<a href="mailto:info@jh2risk.com">info@jh2risk.com</a>



## TranRiskPricing© Quantifies Key Risk Factors

In order to quantify the key risk factors associated with a new investment, JH2 Risk Advisors professionals have developed a proprietary risk scoring model, which measures all key risk factors by:

- ✦ performing a comprehensive, qualitative and quantitative risk assessment of the new transmission investment
- ✦ assigning risk weights to each risk factors
- ✦ finalizing elements of Risk Matrix and deriving cumulative risk score



## TranRiskPricing© Calculates Risk Premium for Incentive Pricing

The core of **TranRiskPricing** is to quantify investment risk factors via JH2's proprietary risk scoring model and translate them into risk premium of the pricing formula. This risk premium can be interpreted as financial compensation both for expected loss and capital reserves held to survive unexpected loss given business uncertainties and regulatory risks.

Capital reserves serve as a venue to provide a stream of cash flow in addition to traditional revenue collection, to absorb loss exposure, and to provide adequate financial liquidity on the balance sheet. They are critical to balance the lengthy nature of transmission investments, such as lengthy permit application processes, intensive capital, and long-term depreciation.

## TranRiskPricing© Facilitates Capital Market Benchmarking

From an investor perspective, any investment can be compared and benchmarked via Return on Equity across the entire capital markets. Our JH2 financial risk specialists have developed a consistent methodology and framework that positions the transmission entity vis a vis other comparable private investments cross multiple industries. Rigorous capital market modeling can then be used to support rate incentive filings with FERC and State PUCs.

The model outputs investment scorecards and recommends solutions that:

- ✦ Create a **TranRiskPricing** benchmarking table across all industries
- ✦ Map underlying investment structures to the benchmarking table
- ✦ Identify the level of risk, resources required and detailed recommendations in alliance with investment best practices from the capital market
- ✦ Assess the likelihood of transmission tariff approval from the federal and state regulators
- ✦ Provide alternative scenarios to adjust for optimal debt/equity structure

## TranRiskPricing© Modifies Corporate Financial Strategy

Based on the outcome of the risk premium and benchmarking comparison, the **TranRiskPricing** model can guide decisions on Debt/Equity ratio, Return on Equity targets, and final complete pricing or new tariffs.

The specifics include:

- ✦ determining optimal financing structure
- ✦ assessing the impact of key risk factors on investment return
- ✦ estimating cost of economic capital
- ✦ calculating reasonable return on equity
- ✦ assisting in final decision making