

Direct Testimony and Schedules  
Richard R. Schrubbe

Before the Minnesota Public Utilities Commission  
State of Minnesota

In the Matter of the Application of Northern States Power Company  
for Authority to Increase Rates for Electric Service in Minnesota

Docket No. E002/GR-19-564  
Exhibit \_\_\_(RRS-1)

**Pension and Benefits Expense**

November 1, 2019

## Table of Contents

I.	Introduction	1
II.	Pension and Benefits Overview	7
III.	Pension Cost Accounting	9
	A. The Nature of Pension Expense	10
	B. Treatment of Gain and Loss Experiences	13
	C. Calculation of Pension Expense under the ACM	21
	D. Calculation of Pension Expense under FAS 87	26
	E. Pension Funding	33
IV.	Pension Assumptions	34
	A. Discount Rate Assumption	36
	B. EROA Assumption	40
V.	Qualified Pension and 401(k) Match Costs	42
	A. Qualified Pension Expense	42
	B. 401(k) Match	46
	C. Qualified Pension Deferred Balances	48
	D. Qualified Pension and 401(k) Match Benefits Summary	50
VI.	Retiree Medical and FAS 112 Long-Term Disability Benefits	51
	A. Retiree Medical	52
	B. FAS 112 Long-Term Disability Benefits	55
	C. Retiree Medical & FAS 112 Long-Term Disability Summary	58
VII.	Benefit Rate Base Assets and Liabilities	59
	A. Overview of the Prepaid Pension Asset	59
	B. Ratemaking Treatment of Prepaid Pension Asset	63
	C. Justification for Including the Net Asset in Rate Base	67

VIII.	Active Health and Welfare Costs	72
IX.	Workers' Compensation FERC 925 Costs	77
X.	Conclusion	80

## Schedules

Resume	Schedule 1
2015-2022 Pension and Benefit Expense Amount	Schedule 2
Approximate Pension Cost Attributable to 2008-2018 Gains and Losses	Schedule 3
FAS 87 and ACM Amortization	Schedule 4
Description of Components and Calculations under ACM and SFAS 87	Schedule 5
XEPP Fund Analysis	Schedule 6
EEI Index Companies	Schedule 7
Determination of Discount Rates and EROA Assumptions	Schedule 8
2020 to 2022 Actuarial Studies	Schedule 9
2020 Actuarial Costs	Schedule 10
Pension Annual Compliance Filing	Schedule 11
Docket No. E002/GR-15-826 DOC IR 2163 and 2164	Schedule 12
Prepaid Pension Asset Support Calculation	Schedule 13
2020 Test Year Health and Welfare O&M	Schedule 14
Medical and Pharmacy Cost Trend	Schedule 15

## Terms and Acronyms

ACM	Aggregate Cost Method
Commission	Minnesota Public Utilities Commission
Company	Northern States Power Company – Minnesota
DB	Defined Benefit
EEI	Edison Electric Institute
ERISA	Employee Retirement Income Security Act
EROA	Expected Return on Assets
FAS	Statement of Financial Accounting Standard
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
IBNR	Incurred But Not Reported
IRC	Internal Revenue Code
LTD	Long-Term Disability
NSPM	Northern States Power Company – Minnesota
PBGC	Pension Benefit Guaranty Corporation
PBO	Pension Benefit Obligation
PTAC	Pension Trust Administrative Committee
PVFB	Present Value of Future Benefits
Xcel Energy	Xcel Energy Inc.
XEPP	Xcel Energy Pension Plan
XES	Xcel Energy Services Inc.

1 **I. INTRODUCTION**

2  
3 Q. PLEASE STATE YOUR NAME AND OCCUPATION.

4 A. My name is Richard Schrubbe. I am the Area Vice-President of Financial  
5 Analysis and Planning for Xcel Energy Services Inc. (XES), which provides  
6 services to Northern States Power Company – Minnesota (NSPM or the  
7 Company).

8  
9 Q. PLEASE SUMMARIZE YOUR QUALIFICATIONS AND EXPERIENCE.

10 A. As Area Vice-President of Financial Analysis and Planning, I am responsible  
11 for overseeing the business area leaders of Energy Supply, Transmission,  
12 Distribution, Gas Engineering & Operations and Corporate Services with  
13 respect to budget planning, reporting, and analysis. I oversee the accounting  
14 for all employee benefits programs, playing a liaison role with the Human  
15 Resources department, external actuaries, and senior management with benefit  
16 fiduciary roles. I am also responsible for coordinating the benefits operations  
17 and maintenance (O&M) and capital budgeting and forecasting processes, as  
18 well as the monthly analysis of actual results against these budgets and  
19 forecasts. A summary of my qualifications, duties and responsibilities is  
20 included as Exhibit\_\_\_(RRS-1), Schedule 1.

21  
22 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

23 A. I discuss the pension plans and other non-cash benefits the Company offers  
24 to its eligible employees and their families, and I present the costs of these  
25 benefits in the multi-year rate plan period, which is the period from 2020-  
26 2022. In addition, I discuss pension cost accounting principles and explain

1 how the Company's pension expense necessarily reflects the cumulative effect  
2 of pension asset gain and loss experiences.

3  
4 I also support the Company's request to include the net rate base increase  
5 associated with its benefit costs. This net rate base increase reflects the  
6 increase associated with the prepaid pension asset, although that amount is  
7 reduced to some extent by the accrued unfunded liability costs associated with  
8 the retiree medical and post-employment benefit costs and accumulated  
9 deferred income taxes. I provide a detailed discussion of the accounting and  
10 ratemaking treatment of these costs, and I demonstrate why this ratemaking  
11 treatment is reasonable.

12  
13 Q. ARE THERE OTHER TOPICS COVERED IN YOUR TESTIMONY OR CHANGES SINCE  
14 YOUR LAST RATE CASE THAT YOU WOULD LIKE TO HIGHLIGHT?

15 A. Yes. First, in our last two rate cases the Commission approved a cap and  
16 deferral mechanism for XES pension expense, as well as a deferral and  
17 amortization mechanism for NSPM pension expense<sup>1</sup>. I quantify the  
18 regulatory assets associated with these deferral mechanisms and explain that  
19 the Company proposes to continue using them to set rates in this current case.  
20 In addition, the Company proposes to amortize the regulatory asset from the  
21 XES pension cap over the three years of the multi-year rate plan. Company  
22 witnesses Mr. Chamberlain and Mr. Halama discuss the appropriateness of  
23 this three-year amortization period.

---

<sup>1</sup> The two deferral mechanisms are necessary because the XES and NSPM pension plans use different accounting methods. I discuss these accounting methods in detail in Section III of my testimony.

1 Second, in Order Point 6 in Docket No. E002/GR-13-868, the Commission  
2 approved the use of a five-year average discount rate for our XES pension  
3 plan under Statement of Financial Accounting Standard (FAS) 87. The  
4 Company still believes that it is appropriate to use the discount rate  
5 established using a single-year bond-matching study, and we reserve the right  
6 to propose such a study as the basis for setting the proper discount rate in  
7 future cases. However, to reduce the potential number of disputed issues in  
8 this case we have used a five-year average discount rate as ordered by the  
9 Commission in our 2013 rate case. I discuss the discount rate and other  
10 pension assumptions in detail in Section IV of my testimony.

11  
12 Finally, while I do not discuss the 2008 market loss at the level of detail  
13 provided in our last two cases, in Section III of my testimony I discuss  
14 pension accounting in detail, including the phase in and amortization of  
15 pension asset gain and loss experiences.

16  
17 Q. IS ANY OTHER COMPANY WITNESS ADDRESSING PENSION AND BENEFIT  
18 ISSUES?

19 A. Yes. Company witness Ms. Ruth K. Lowenthal discusses the cash  
20 compensation offered by the Company, as well as the steps the Company has  
21 taken to help mitigate pension and benefit cost increases. In addition,  
22 Company witness Mr. Evan Inglis discusses the appropriateness of the  
23 Company's pension investment strategy.

1 Q. WHAT ORDER POINTS FROM COMMISSION ORDERS DO YOU ADDRESS IN YOUR  
2 TESTIMONY?

3 A. Table 1 below lists the order points I respond to from Commission Orders in  
4 rate cases (Docket No. E002/GR-13-868) and (Docket No. E002/GR-12-  
5 961). Table 1 lists the page numbers of my testimony where each is addressed.

**Table 1**  
**Order Point Requirements**

Docket No. Order Point	Requirement	Page Numbers
13-868 7	The Company shall apply the rolling five-year average FAS 87 discount rate when determining the XES Plan cost subject to deferral (or reversal) in subsequent years (i.e., non-rate-case test years) as the 2012 mitigation established in Docket No. E002/GR-12-961 continues.	p. 36
13-868 10	The qualified pension asset and associated deferred-tax amounts shall be included in rate base. For rate-base purposes, the pension asset is to reflect the cumulative difference between actual cash deposits made by the Company reduced by the recognized qualified pension cost determined under the ACM/FAS 87 methods since plan inception, not to exceed the Company's filed request. The Company shall provide a detailed compliance filing which explains the calculated amount within ten days of the Commission's decision.	p. 63 Schedule 13
13-868 13	The discount rate used to calculate retiree medical benefit costs for ratemaking purposes shall be set to equal 5.08%, the five-year average of the FAS 106-based discount rates.	p.51-53
13-868 14	Any amount by which the qualified pension expense allowed in rates exceeds future years' qualified pension expense (calculated using the Commission-approved discount-rate point of reference) the Company shall apply toward the recovery of the accumulated deferred XES Plan costs. "Future years" includes 2015, and each subsequent year's qualified pension expense if not a rate-case test year. The recoverable XES Plan expense amount shall be calculated using the proximate measurement date appropriate for each operating year (12/31/2013 for 2014; 12/31/2014 for 2015, etc.) until the next rate case. The Company shall file annual compliance reports which provide its pension plans' cost-calculation reports, the XES Plan accumulated deferred balance, and the excess rate-level recovery applied toward satisfying the deferral. Deferred amounts shall not be included in rate base.	p. 50-51 Schedule 11
12-961 37	The Company shall not be permitted to include a compensating return on the pension's unamortized asset loss balance.	p. 49
12-961 40	In future rate case filings, Xcel shall include for each pension plan schedules of its 2008 market loss amortization, for the entire amortization period, until the 2008 market loss amortization has been extinguished.	P. 19 Schedule 3

1 Q. HOW IS THE REMAINDER OF YOUR TESTIMONY ORGANIZED?

2 A. I present the remainder of my testimony in the following sections:

- 3 • Section II, *Pension and Benefits Overview*, provides a summary of the  
4 pension and benefit costs included in our multi-year rate request.
- 5 • Section III, *Pension Cost Accounting*, discusses pension accounting  
6 principles and how the Company calculates its pension expense.
- 7 • Section IV, *Pension Assumptions*, presents the primary assumptions used  
8 to calculate our pension costs in this case.
- 9 • Section V, *Qualified Pension and 401(k) Match Costs*, quantifies the test  
10 year and multi-year rate plan expense amounts.
- 11 • Section VI, *Retiree Medical and FAS 112 Long-Term Disability Benefits*,  
12 presents information and costs related to our request for recovery of  
13 post-retirement healthcare and long-term disability benefits.
- 14 • Section VII, *Benefit Rate Base Assets and Liabilities*, discusses ratemaking  
15 treatment of both the Company's prepaid benefit costs and unfunded  
16 accrued liability costs.
- 17 • Section VIII, *Active Health and Welfare Costs*, provides details related to  
18 the active healthcare costs included in our rate request.
- 19 • Section IX, *Workers' Compensation FERC 925 Costs*, provides details  
20 related to the workers' compensation costs included in our rate request.
- 21 • Section X, *Conclusion*, summarizes the Company's request for recovery  
22 of pension and benefit-related costs.

1 **II. PENSION AND BENEFITS OVERVIEW**

2  
3 Q. WHAT TYPES OF COSTS ARE INCLUDED IN THE COMPANY'S PENSION AND  
4 BENEFITS REQUEST?

5 A. With the exception of workers' compensation costs discussed in Section IX of  
6 my testimony, our pension and benefits costs are recorded in FERC Account  
7 926. The Company has grouped its pension and benefit costs into three  
8 categories based on similar budgeting practices and cost recognition  
9 requirements. The three categories are: (1) actuarial costs; (2) health and  
10 welfare costs; and (3) other retirement costs.

11  
12 Q. TO PROVIDE CLARITY, PLEASE DESCRIBE HOW DOLLAR AMOUNTS IN YOUR  
13 TESTIMONY ARE PRESENTED.

14 A. Unless specifically indicated otherwise, all of the dollar values presented in my  
15 testimony are presented at the NSPM electric, state of Minnesota level.

16  
17 Q. PLEASE PROVIDE A SUMMARY OF THE PENSION AND BENEFIT COSTS INCLUDED  
18 IN THE COMPANY'S MULTI-YEAR RATE REQUEST.

19 A. Table 2 below sets forth the benefit amounts approved in our 2013 rate case,  
20 the forecasted 2019 expense amounts, and the forecast amounts for each year  
21 of the multi-year rate plan, (the 2015 rate case was settled on an overall  
22 revenue requirements basis, so there was no Commission approval of specific  
23 benefit amounts).

**Table 2**  
**Pension and Benefit Expense Summary (\$)**

<b>FERC Account 926 Pension and Benefit Costs for NSPM Electric O&amp;M, State of Minnesota</b>					
<b>FERC 926 Benefit Type</b>	<b>Amount Approved in Docket No. 13-868</b>	<b>2019 Forecast</b>	<b>2020 Test Year</b>	<b>2021 Plan Year</b>	<b>2022 Plan Year</b>
<b>Actuarial Costs</b>					
Qualified Pension (1)	20,923,341	21,398,739	20,956,503	20,378,317	19,780,720
Deferred Pension Amortization			5,881,632	5,881,632	5,881,632
Nonqualified Pension		846,478			
FAS 106 Retiree Medical (2)	2,202,778	1,103,990	1,266,772	1,138,526	1,040,350
FAS 112 LTD	171,948	(73,979)	110,266	102,611	96,468
<b>Total Actuarial Costs</b>	<b>23,298,067</b>	<b>23,303,673</b>	<b>28,215,172</b>	<b>27,501,086</b>	<b>26,799,170</b>
<b>Health &amp; Welfare</b>					
Active Health Care	32,207,553	33,530,876	34,547,977	35,966,484	37,505,915
Misc Ben Programs, Life, LTD	3,135,796	4,014,610	3,875,486	3,925,296	3,992,836
<b>Total Health &amp; Welfare</b>	<b>35,343,349</b>	<b>37,545,486</b>	<b>38,423,462</b>	<b>39,886,575</b>	<b>41,489,982</b>
<b>Other Retirement</b>					
401(k) Match	8,012,615	9,259,666	9,313,718	9,553,390	9,809,095
Deferred Comp Match	32,807	47,646	52,453	56,301	60,380
NMC Employer Ret. Contr.	763,161	945,369	816,918	840,806	865,425
Ret. & Comp Consulting	673,136	544,143	487,355	487,366	488,222
<b>Total Other Retirement</b>	<b>9,481,719</b>	<b>10,768,377</b>	<b>10,670,443</b>	<b>10,937,862</b>	<b>11,223,122</b>
<b>Total FERC 926</b>	<b>68,123,136</b>	<b>71,617,536</b>	<b>77,309,078</b>	<b>78,325,523</b>	<b>79,512,274</b>

(1) Reflects NSPM calculated under the Aggregate Cost Method using a 20 year amortization. XES amount calculated using the 5-year average discount rate and the amount (deferred) / amortized resulting from XES pension costs being above or below the 2011 cap amount approved by the Commission in Docket No. E002/GR-12-961 and continued in Docket No. E002/GR-13-868. For 2020-2022 the Company has compared the amount to the 2019 forecasted expense, which is the amount that the company is seeking to reset the cap to in this rate filing.

(2) Calculated using the 5-year average discount rate.

1 Q. IS THE COMPANY SEEKING TO RECOVER THE FORECASTED PENSION AND  
2 BENEFITS EXPENSE AS SHOWN IN TABLE 2 AS PART OF ITS MULTI-YEAR RATE  
3 PLAN?

4 A. Yes. Company witness Mr. Benjamin C. Halama has incorporated the  
5 forecasted amounts into the 2020 test year and the 2021 and 2022 plan year  
6 revenue requirements. As discussed in detail throughout my testimony, our  
7 forecasts of pension and benefit costs included in FERC Account 926 are  
8 formulaic, calculated in accordance with accounting rules and standards, based  
9 on actuarial assumptions specific to the Company, and in some cases reflect  
10 specific regulatory treatment applied in prior Commission Orders.

11

12 Q. HOW DO THE AMOUNTS OF PENSION AND BENEFIT EXPENSE IN 2020, 2021,  
13 AND 2022 COMPARE TO THE ACTUAL AMOUNTS INCURRED IN PRIOR YEARS?

14 A. Exhibit\_\_\_(RRS-1), Schedule 2 to my testimony contains a comparison of the  
15 pension and benefit expense amounts in 2020-2022 to the amounts of actual  
16 expense in prior years and the forecasted amount for 2019.

17

### 18 III. PENSION COST ACCOUNTING

19

20 Q. WHAT TOPIC DO YOU DISCUSS IN THIS SECTION OF YOUR TESTIMONY?

21 A. In this section I discuss pension accounting principles and describe how the  
22 Company calculates its test year pension expense.

23

24 Q. IN ORDER TO ESTABLISH THE CONTEXT FOR YOUR DISCUSSION OF THE  
25 CALCULATION OF PENSION EXPENSE, PLEASE DESCRIBE THE QUALIFIED  
26 PENSION PLANS THE COMPANY OFFERS.

1 A. The Company has two qualified pension plans: the NSPM Plan and the XES  
2 Plan. Employees of NSPM are eligible to participate in the NSPM Plan;  
3 employees of our service company subsidiary, XES, are eligible to participate  
4 in the XES Plan.

5 Q. ARE THE PENSION COSTS ATTRIBUTABLE TO EACH PLAN ACCOUNTED FOR IN  
6 THE SAME WAY?

7 A. No. Pension costs under the NSPM Plan are determined under the Aggregate  
8 Cost Method (ACM), whereas pension costs for the XES Plan are determined  
9 in accordance with FAS 87.<sup>2</sup> The history of the Company's use of these two  
10 different accounting methods is explained on page 21 and as I explain below;  
11 the ultimate goal of both methods is the same – to provide an actuarially  
12 sound basis to calculate and recover over the course of an employee's career  
13 the amount of money that will be necessary to satisfy the Company's pension  
14 obligation to that employee. In effect, both methods allow the Company to  
15 reflect a current expense associated with a future liability.

16

17 **A. The Nature of Pension Expense**

18 Q. IS PENSION EXPENSE SIMPLY A CASH OUTLAY IN THE TEST YEAR, LIKE MANY  
19 OTHER COMPONENTS OF OPERATION AND MAINTENANCE EXPENSE?

20 A. No. Pension expense represents an accrual for a future liability rather than the  
21 cash to pay benefits in a given year. Thus, pension expense is more similar to  
22 our nuclear decommissioning accrual, which is an expense in our cost of  
23 service, than it is to, say, contractor expense for our vegetation management,  
24 which more closely represents cash that flows out the door in a given year.

25

---

<sup>2</sup> In 2009 FAS 87 was renamed Accounting Standards Codification 715-30, but I will continue to refer to the standard in this testimony as FAS 87 for ease of reference.

1 Q. WHY IS THE DISTINCTION BETWEEN A PRESENT ACCRUAL AND A PRESENT  
2 CASH OUTLAY IMPORTANT?

3 A. A more current cash outlay, such as vegetation management (we still use  
4 accrual accounting for this cost), is not materially affected by a number of  
5 assumptions about longer term future conditions, but only by timing  
6 differences in the billing for the costs. In contrast, the current accrual for a  
7 substantial and distant future liability is affected by both past events and future  
8 forecasts. We must know what happened in the past and must have a forecast  
9 of what will happen in the future in order to derive an accurate measure of the  
10 current year expense associated with that future liability.

11

12 Q. WHY ARE PAST EVENTS TAKEN INTO CONSIDERATION FOR PURPOSES OF  
13 CALCULATING PENSION EXPENSE?

14 A. A fundamental component of pension expense is the experience from prior  
15 years. That is, the current year's pension expense is determined by knowing  
16 the existing value of the assets in the trust, as well as the forecasted future  
17 liability. To the extent the existing value of the assets is higher than initially  
18 forecasted, the level of expense is reduced, as there is less future cost to be  
19 recognized in the current period. To the extent the existing value of the assets  
20 is lower than initially forecast, then the expense level is higher.

21

22 Q. WHAT IS THE PROCESS FOR TAKING THE PAST EVENTS INTO ACCOUNT?

23 A. The elements used to calculate pension costs are established at the beginning  
24 of each year based on actuarial studies that account for factors such as the  
25 expected salary increases, expected mortality rates, the Expected Return on  
26 Assets (EROA), the discount rate and other factors. At the end of the year,

1 the assumptions are trued up to actual experience, and the differences give  
2 rise to gains or losses.

3  
4 Q. WHY IS IT NECESSARY TO TRUE-UP THE PROJECTIONS TO ACTUAL  
5 EXPERIENCE?

6 A. The Company makes projections so that it can reflect the most accurate  
7 forward-looking level of pension expense on its income statement. For  
8 example, our projection of future pension liability is based on our best  
9 estimate of how long employees will stay with the Company because pension  
10 benefits are designed to grow with years of service. But circumstances change  
11 over the course of a year and the assumptions we made at the beginning of the  
12 year may have changed. To make our pension expense projections for the  
13 following year as accurate as possible, we incorporate the differences between  
14 the projections and actual experience from the prior years in our calculation of  
15 annual pension expense.

16  
17 Q. WHAT DO YOU MEAN WHEN YOU SAY THAT THE COMPANY ACCOUNTS FOR  
18 THE CHANGES THAT HAVE OCCURRED?

19 A. Pension accounting systematically tracks the differences between the Year 1  
20 forecast assumptions and the Year 1 actual experience, and then it includes a  
21 portion of that difference into the Year 2 pension expense as a gain or loss. (I  
22 explain in the next part of my testimony why only a portion is incorporated  
23 into the Year 2 pension expense calculation.) Deviations that reduce the level  
24 of the Present Value of Future Benefits (PVFB) are gains. Deviations that  
25 increase the PVFB are losses. The treatment of cumulative gain and loss  
26 experiences is a key component of the annual pension expense calculation, as I  
27 will discuss in the next subsection of my testimony.

1        **B.     Treatment of Gain and Loss Experiences**

2    Q.    WHAT FOUNDATIONAL CONCEPTS ARE NECESSARY TO UNDERSTAND HOW  
3        GAIN AND LOSS EXPERIENCES ARE INCORPORATED INTO THE CALCULATION  
4        OF CURRENT PENSION EXPENSE?

5    A.    The first concept is that asset gains and losses must be distinguished from  
6        liability gains and losses. I will explain below the difference between those  
7        types of gains and losses.

8  
9        The second concept involves the phase-in of asset gains and losses. As I will  
10       discuss in more detail below, asset gains and losses are phased into an  
11       amortization “pool,” for lack of a better term, over a five-year period.  
12       Liability gains and losses are not phased in, but instead are placed into the  
13       amortization pool in a single year.

14  
15       The third concept involves amortization. FAS 87 asset and liability gains and  
16       losses that enter the amortization pool are amortized over the remaining  
17       service lives of existing employees if they fall outside a “corridor.” If the FAS  
18       87 gains or losses are within the corridor, they are not amortized. I will  
19       discuss the corridor and the mechanics of the amortization in more detail  
20       below. ACM gains and losses are treated a bit differently, but the concepts are  
21       similar. As with FAS 87, asset gains and losses are phased in over a five-year  
22       period. After accounting for the phase-in of asset gains and losses, the  
23       Company calculates the difference between the market-related value of the  
24       pension plan assets and the PVFB owed by the Company, and the difference  
25       is spread over the remaining service lives of existing employees. As I will  
26       explain below, this is not an amortization in the same sense as the FAS 87

1 amortization, but it achieves similar results in that it results in the spreading of  
2 unrecognized gains and losses over a period of years.

3  
4 Q. STARTING WITH THE FIRST CONCEPT YOU MENTIONED, PLEASE EXPLAIN THE  
5 DISTINCTION BETWEEN ASSET GAINS AND LOSSES AND LIABILITY GAINS AND  
6 LOSSES.

7 A. Asset gains or losses arise when the actual returns on the pension trust assets  
8 in a given year are greater than or lesser than the expected return on those  
9 assets. Suppose, for example, that the plan expects a 7 percent return on its  
10 pension trust assets, which total \$1 billion. The expected return for that year  
11 would be \$70 million. If the actual return in that year is 9 percent, the asset  
12 gain will be \$20 million. Of course, the opposite can also occur. If the  
13 expected return is 7 percent and the actual return on the assets is 5 percent,  
14 the plan suffers a \$20 million asset loss.

15  
16 Liability gains and losses arise when the other components of pension expense  
17 differ from expectations. Those components include such things as the  
18 discount rate, the expected number of retirements, and wage increases. For  
19 example, if the Company assumes a 4 percent discount rate at the beginning  
20 of the year but the actual discount rate measured at year end for the next year  
21 turns out to be 5 percent, the Company will have a liability gain because the  
22 higher discount rate reduces the amount the Company must set aside to satisfy  
23 future pension liabilities.

24  
25 Q. IS THE DISTINCTION BETWEEN ASSET GAINS AND LOSSES AND LIABILITY GAINS  
26 AND LOSSES IMPORTANT?

1 A. Yes. The distinction is important because, as I will discuss in more detail  
2 below, the asset gains and losses are phased in over time, whereas the liability  
3 gains and losses are not. Therefore, they must be tracked separately.

4

5 Q. HAVE YOU PROVIDED ANY EXAMPLES OF THE DISTINCTION BETWEEN ASSET  
6 GAINS AND LOSSES AND LIABILITY GAINS AND LOSSES?

7 A. Yes. Exhibit\_\_\_\_(RRS-1), Schedule 3 shows the asset gains and losses and the  
8 liability gains and losses from 2008 to 2018.

9

10 Q. WHEN THE COMPANY HAS ASSET GAINS OR LIABILITY GAINS, DOES IT  
11 WITHDRAW THOSE AMOUNTS FROM THE TRUST AND TREAT THEM AS  
12 EARNINGS?

13 A. No. Federal law requires that all of the gains and losses stay within the  
14 pension trusts, which means that they affect the amount of pension expense in  
15 subsequent years. Generally speaking, if there is an asset or liability gain, it  
16 reduces the Company's pension expense in the following years. If there is an  
17 asset or liability loss, it increases pension expense in the following years.  
18 Thus, the Company treats gains and losses symmetrically in the sense that  
19 both must remain in the pension trust and both affect future pension expense.

20

21 Q. TURNING TO THE SECOND CONCEPT, PLEASE EXPLAIN WHAT YOU MEAN BY  
22 THE "PHASE IN" OF GAINS OR LOSSES.

23 A. The term "phase in" is used to describe the process of moving asset gains or  
24 losses into an amortization pool. Under FAS 87 and the ACM, the asset gains  
25 or losses are incorporated into the calculation of pension expense over a  
26 period of five years. Thus, 20 percent of a gain or loss is phased into the  
27 amortization pool during the first year after the gain or loss occurs, another 20

1 percent is phased into the amortization pool during the second year after the  
2 gain or loss occurs, and so forth until the fifth year, when the full amount of  
3 the gain or loss is phased in. The portion of gains and losses that enter the  
4 amortization pool are then amortized over a specific period of years if they  
5 satisfy the criteria I discuss below. Unlike asset gains or losses, liability gains  
6 and losses are not phased in.

7  
8 Q. WHY ARE ASSET GAINS AND LOSSES PHASED IN BUT NOT LIABILITY GAINS AND  
9 LOSSES?

10 A. The assumptions used to establish pension liability (e.g., mortality rates,  
11 discount rates, etc.) typically do not vary greatly from year to year, and  
12 therefore, the drafters of FAS 87 did not consider it necessary to require the  
13 phase-in of liability gains and losses. In contrast, the market returns on  
14 pension fund assets can vary greatly from year to year. Because of the effects  
15 that such volatility would have on businesses' income statements, the drafters  
16 of FAS 87 decided that it was appropriate to phase-in market gains and losses.

17  
18 Q. ARE EACH YEAR'S GAINS OR LOSSES CONSIDERED IN ISOLATION?

19 A. No. After the phase-in is completed, the current year's gains and losses are  
20 aggregated with the previously accumulated gains and losses.

21  
22 Q. PLEASE DISCUSS THE THIRD CONCEPT YOU MENTIONED – THE AMORTIZATION  
23 OF GAINS AND LOSSES.

24 A. In addition to phasing the asset gains or losses into the amortization pool, the  
25 Company must undertake an analysis to determine whether it will actually  
26 amortize those gains or losses.

1 Q. HOW DOES THE COMPANY DETERMINE WHETHER IT WILL AMORTIZE GAINS  
2 OR LOSSES?

3 A. It depends on which plan is under review, because the analysis for FAS 87 is  
4 not the same as the analysis for the ACM. For FAS 87, which governs the  
5 XES Plan, the Company aggregates its current year's gains or losses with the  
6 other accumulated gains or losses to calculate a net unamortized gain or loss.  
7 That net unamortized gain or loss is then compared to the present value of the  
8 projected benefit obligation (PBO) and to the market-related value of the  
9 assets in the pension trust. If the net unamortized gain or loss is outside a 10-  
10 percent corridor – that is, if it is more than 10 percent of the greater of the  
11 PBO or the market-related value of the trust assets – the Company must  
12 amortize that net gain or loss. If the net unamortized gain and loss is within  
13 the corridor, amortization does not occur.

14

15 If amortization of the unrecognized gains or losses is required, the  
16 amortization amount is equal to the amount of the unrecognized gain or loss  
17 in excess of the corridor divided by the average remaining future service of the  
18 active participants in the plan. For the Company's FAS 87 plan this is  
19 approximately 11 years.

20

21 For the ACM, which governs the NSPM Plan, the Company simply compares  
22 the market-related value of the pension trust assets to the PVFB. If the  
23 market-related value of the assets is greater than the PVFB, the plan is  
24 overfunded and there is no pension expense. Thus, there is nothing to be  
25 amortized. If the market value is less than the PVFB, the plan is underfunded,  
26 which means there is pension expense that is amortized over the remaining  
27 service lives of the employees within the actuarial formula.

1 Note, however, that I am using the term “amortization” as a type of  
2 shorthand insofar as the ACM is concerned. The difference between the  
3 market value of trust assets and the PVFB is not truly amortized in the sense  
4 that the amount is established in Year 1 and then that amount is fixed and  
5 recovered according to a schedule that provides for annual payments over the  
6 next several years. Instead, the Company undertakes the following process  
7 each year:

- 8 1) it calculates the difference between the market-related value of the  
9 assets and the PVFB;
- 10 2) if the PVFB exceeds the market-related value, the Company calculates  
11 the number of years over which to recover the difference; and
- 12 3) the difference is divided by the number of years to determine the  
13 amount of pension expense that would need to be recovered in the  
14 current year in order to fund the shortfall.

15  
16 In Year 2, however, this entire process is repeated, and the Company comes  
17 up with a new shortfall amount and a new period over which to fund it. The  
18 amount and the schedule from Year 1 are no longer relevant, because the Year  
19 2 calculation “resets” the amount and the period over which the amount is to  
20 be funded.

21  
22 In short, prior years’ experience, whether positive or negative, is incorporated  
23 into the calculation of the current period recognition of pension expense.

24 Exhibit\_\_\_\_(RRS-1), Schedule 4 contains a decision tree for FAS 87 and a  
25 decision tree for the ACM. Both show the process for determining whether  
26 to amortize gains or losses.

1 Q. ORDER POINT 40 OF THE COMMISSION'S SEPTEMBER 3, 2013 ORDER IN  
2 DOCKET NO. E002/GR-12-961 IS RELATED TO PRIOR PERIOD GAINS AND  
3 LOSSES. IT REQUIRES THE COMPANY TO "INCLUDE FOR EACH PENSION PLAN  
4 SCHEDULES OF ITS 2008 MARKET LOSS AMORTIZATION, UNTIL THE 2008  
5 MARKET LOSS AMORTIZATION HAS BEEN EXTINGUISHED." IS THE COMPANY  
6 PROVIDING THAT INFORMATION?

7 A. Yes. Exhibit\_\_\_(RRS-1), Schedule 3 shows the estimated 2008 Market Loss  
8 amortization by year and plan, as well as the Company's experience in each  
9 year since 2008. Schedule 3 also depicts the phase-in of the asset gains or  
10 losses, as well as the amortization of the net unamortized balances of gains  
11 and losses, with the acknowledgement that our effort to break apart the  
12 NSPM Plan provides a similar look but against a different construct than the  
13 look at the FAS 87 tracked gains and losses.

14

15 Q. WHY DOES SCHEDULE 3 NOT SHOW THE 2008 MARKET LOSS AMORTIZATION  
16 UNTIL IT HAS BEEN EXTINGUISHED, AS DIRECTED BY ORDER POINT 40?

17 A. In accordance with the requirements of ACM and FAS 87 accounting  
18 standards, the amortization amount is re-determined each year as described  
19 below and does not follow a fixed schedule with a pre-determined end.

20

21 For FAS 87, each year the remaining amortizable gain or loss is divided by the  
22 average remaining service period for active employees. The average remaining  
23 service period for active employees is approximately eleven years and is re-  
24 determined each year based on the active participants in the plan. With an  
25 open plan that allows new hire participation, the average remaining service  
26 period has remained relatively constant and is expected to continue to be  
27 approximately eleven years. Since the denominator of the amortization

1 equation remains approximately eleven in all years, the amortization amount  
2 will gradually decline, but will never be fully amortized. This is similar to what  
3 would happen if a 30-year mortgage was re-financed each year into a new 30-  
4 year mortgage (the payments will decline, but the payment period is reset each  
5 year to 30 years)

6  
7 For ACM, the concept is the same as FAS 87, except instead of amortizing  
8 gains and losses, the unfunded liability is amortized each year. The  
9 amortization period for ACM is determined each year using the 20-year  
10 amortization basis, which at a 7.10 percent discount rate is approximately  
11 eleven years. Using the same amortization factor each year leads to declining  
12 amortization payments, but because the amortization factor is reset each year,  
13 the amount will not be fully extinguished until there is no unfunded liability.

14 Schedule 3 shows the first twenty years of payments for both FAS 87 and  
15 ACM.

16  
17 Q. DO THE AMOUNTS ON SCHEDULE 3 SET FORTH THE COMPANY'S PENSION  
18 EXPENSE IN THE TEST YEAR?

19 A. No. The discussion of pension expense up to now has been only about how  
20 the pension asset gain and loss experiences are recorded and carried forward  
21 for incorporation into the current year's pension expense. In Section C below  
22 I will describe how the current year's pension expense is calculated under the  
23 ACM and FAS 87, and how that current pension expense incorporates past  
24 pension asset gain and loss experiences. I will also explain how the current  
25 pension expense incorporates liability gains and losses.

1           **C.     Calculation of Pension Expense under the ACM**

2    Q.   WHY DOES THE NSPM PLAN USE THE ACM TO ACCOUNT FOR PENSION  
3       EXPENSE?

4    A.   NSPM began using the ACM to calculate pension expense in 1975.  Although  
5       FAS 87 became the new standard for pension accounting for financial  
6       reporting purposes in 1987, it was made subject to the effects of rate  
7       regulation as provided for by FAS 71, which allowed regulated entities such as  
8       the NSPM Plan to reflect the “rate actions of a regulator” and the “effects of  
9       the rate-setting process” by regulatory agencies, such as the Commission.  The  
10      authority provided by FAS 71 allowed the NSPM Plan to continue using the  
11      ACM for ratemaking purposes, as it had before 1987, and the Commission  
12      approved this continued use.

13  
14   Q.   PLEASE SUMMARIZE THE ACM AND EXPLAIN HOW PENSION COSTS ARE  
15       CALCULATED UNDER THAT METHOD.

16   A.   The ACM is based on a normalized level of long-term cash funding  
17       requirements measured as a constant percentage of payroll.  Under the ACM,  
18       the pension cost is the normalized amount that would need to be paid into the  
19       pension fund each year to fund earned benefits.  Based on specific actuarial  
20       assumptions such as the discount rate, projected salary levels, and mortality,  
21       the PVFB is calculated and compared to the phased-in market-related value of  
22       plan assets.  The difference between the PVFB and the market value of assets  
23       is the unfunded liability that must be funded over the future working lives of  
24       current employees.  I have included a summary of the ACM in  
25       Exhibit\_\_\_\_(RRS-1), Schedule 5, along with a comparison to the FAS 87  
26       method for calculating pension expense.

1 Q. PLEASE PROVIDE AN EXAMPLE OF HOW THE ACM WORKS.

2 A. Suppose the Company determines, based on actuarial studies, that it will  
3 ultimately need \$3 billion to fund its pension liability, which is the PVFB. If  
4 the market value of assets in the Company's NSPM Plan trust is currently \$2.5  
5 billion, there is a \$500 million difference that will need to be funded. The  
6 ACM requires that the Company fund that amount based on the period  
7 approved by the Commission or the remaining future working lives of its  
8 employees, which is approximately 11 years. The Company then sets the  
9 pension expense at a levelized percentage of payroll based on the amount  
10 needed and the time remaining to fund the pension liability.

11

12 Q. HOW ARE THE PENSION ASSET GAIN AND LOSS EXPERIENCES INCORPORATED  
13 INTO THE ACM CALCULATION?

14 A. Recall that the ACM is calculated by comparing asset values to the PVFB.  
15 Thus, if there is an asset gain from the prior year, the phased-in amount of  
16 that asset gain is added to the market-related value of the assets, and if there is  
17 an asset loss, the phased-in amount of that loss is subtracted from the market-  
18 related value of the assets. Insofar as the PVFB is concerned, if there is a  
19 liability gain from the prior year, the PVFB is reduced by that amount. If the  
20 plan has a liability loss from the prior year, the PVFB grows by that amount.  
21 The difference between the asset value and the PVFB after incorporating the  
22 asset and liability gains and losses is the amount that is placed into the  
23 amortization pool, and netted with the cumulative unrecognized gain and loss  
24 experiences.

1 Q. PLEASE PROVIDE AN EXAMPLE OF HOW THE CALCULATION WORKS.

2 A. Consider the example set forth earlier – the market value of assets is \$2.5  
3 billion and the PVFB is \$3.0 billion, which creates a funding obligation of  
4 \$500 million in Year 1. Now suppose the following events occur:

5 • The actuarially determined EROA for Year 1 was 7 percent, but the  
6 fund actually earned 6 percent. In that instance, the fund would have  
7 an asset loss of \$25 million ( $\$2.5 \text{ billion} \times .01 = \$25 \text{ million}$ ).

8 • The actual discount rate in Year 1 was 25 basis points higher than the  
9 actuaries had assumed, which reduced the PVFB by \$15 million. Thus,  
10 the fund has a liability gain of \$15 million for Year 1.

11 • The pension fund paid out \$175 million in benefits in Year 1, which is  
12 exactly equal to the expected earnings on the plan's assets during that  
13 year ( $\$2.5 \text{ billion assets} \times .07 \text{ EROA} = \$175 \text{ million}$ ).

14

15 Because the amounts paid out as benefits equal the EROA, the only changes  
16 that need to be incorporated in the Year 2 pension expense are the asset loss  
17 and the liability gain. The Year 1 asset loss was \$25 million, but under the  
18 phase-in rules, only \$5 million of that is reflected in the market value of assets  
19 in Year 2. On the other hand, the entire \$15 million liability gain is recognized  
20 in Year 2, so the Year 2 asset value drops by \$5 million and the Year 2 PVFB  
21 drops by \$15 million. Now the difference between the market value of the  
22 assets and the PVFB is \$490 million instead of \$500 million. That \$490  
23 million is then spread over the amortization period approved by the  
24 Commission.

1 Q. IN THAT EXAMPLE, WHAT HAPPENS TO THE ASSET LOSSES THAT HAVE NOT  
2 BEEN PHASED IN AND AMORTIZED YET?

3 A. The amount is reflected on the Company's books as an increase to the liability  
4 offset by a regulatory asset, resulting in no change to the net balance sheet  
5 amount of the pension plan. As discussed earlier, an additional amount of the  
6 asset losses will be phased into the amortization pool each year for the next  
7 four years and will reduce the regulatory asset by a corresponding amount  
8 each year, all else being equal.

9

10 Q. THE NSPM PLAN CURRENTLY HAS PRIOR-PERIOD ASSET LOSSES AND PRIOR-  
11 PERIOD LIABILITY LOSSES, BOTH OF WHICH INCREASE THE AMOUNT OF  
12 PENSION EXPENSE IN THE CURRENT YEAR. HAVE THE COMPANY'S CUSTOMERS  
13 BENEFITED FROM ASSET GAINS AND LIABILITY GAINS IN THE PAST?

14 A. Yes. For many years the Company had significant gains because its pension  
15 plan investments benefited from a significant and prolonged upward market  
16 movement, and customers reaped the benefits through market gains that  
17 exceeded the EROA. Mr. Inglis discusses the Company's pension plan  
18 investments in more detail in his testimony.

19

20 Q. IS THE COMPANY ASKING ITS CUSTOMERS TO RESTORE LOSSES FROM PRIOR  
21 YEARS?

22 A. No. We are simply calculating the current year's pension expense, which is  
23 affected by cumulative gain and loss experiences. Expense is determined by  
24 prior experience, and customers have benefitted from the prior gains.  
25 Therefore, it is reasonable, appropriate, and necessary to reflect both prior-  
26 period gain and loss experiences in current pension expense.

1 Q. HOW HAVE THE PRIOR GAIN EXPERIENCES BEEN INCORPORATED INTO THE  
2 COMPANY'S PENSION EXPENSE?

3 A. Prior gain experiences have been incorporated in the same way the prior loss  
4 experiences were incorporated. For the NSPM Plan, the asset gains and  
5 liability gains reduced the amount that needed to be funded, which reduced  
6 the pension expense charged to customers. For the XES Plan, the asset gains  
7 and liability gains have offset the service costs and interest costs that our  
8 customers would otherwise have paid in rates.

9

10 Q. DO YOU HAVE DATA TO SHOW HOW CUSTOMERS HAVE BENEFITED FROM  
11 PENSION ASSET GAINS?

12 A. Yes. Exhibit\_\_\_(RRS-1), Schedule 6 quantifies the significant benefits that  
13 the Company's pension assets have provided to customers. Schedule 6 shows  
14 the Xcel Energy Pension Plan (XEPP) Trust activity since its inception in  
15 1950. Although Schedule 6 reflects more than just the NSPM Plan, it does  
16 demonstrate the overall value of the pension assets, which include the NSPM  
17 assets.<sup>3</sup> Since 1950, the Company has contributed approximately \$1.3 billion  
18 into the trust while earning approximately \$4.0 billion in investment returns,  
19 which helped pay for approximately \$4.2 billion in payments to employees.  
20 For many years these asset returns enabled the Company to recognize pension  
21 benefit costs at or very close to zero and to make no pension contributions.  
22 These low or nonexistent pension expense amounts were reflected in our rate  
23 cases, which means that customers paid much less in annual pension cost than  
24 they would have in the absence of the pension asset gains.

---

<sup>3</sup> As of December 31, 2018, the NSPM Plan owned 52 percent of the total XEPP plan assets.

1 Q. WHAT HAS THE COMPANY DONE WITH THOSE GAINS?

2 A. By law, earnings on pension trust assets cannot be removed from the trust  
3 fund. Therefore, the net gains on the pension asset have been used to reduce  
4 the pension expense charged to our customers and mitigated cash funding  
5 requirements.

6

7 Q. IS THERE ANY OTHER WAY IN WHICH CUSTOMERS HAVE BENEFITED FROM THE  
8 PENSION ASSET GAINS?

9 A. Yes. For more than 50 years the Company's pension plan has provided a  
10 market-competitive employee benefit, which allowed us to attract and retain  
11 employees that helped us build, operate, and maintain the electrical system  
12 that continues to provide safe, reliable electric service. The pension asset  
13 gains have helped the Company provide that benefit at a much lower cost  
14 than would have been possible without the asset gains.

15

16 **D. Calculation of Pension Expense under FAS 87**

17 Q. PLEASE PROVIDE AN OVERVIEW OF FAS 87.

18 A. FAS 87 is an accounting standard adopted by the Financial Accounting  
19 Standards Board (FASB) in 1987 to govern employers' accounting for  
20 pensions. Under FAS 87, pension cost is generally made up of five  
21 components of costs but a sixth component can be required provided certain  
22 criteria are met during the year. The five main components of FAS 87  
23 pension cost are:

- 24 1) the present value of pension benefits that employees will earn during  
25 the current year (service cost);  
26 2) increases in the present value of the PBO that plan participants have  
27 earned in previous years (interest cost);

- 1           3) expected investment earnings during the year on the pension plan
- 2           assets, or Expected Return On Assets (EROA);
- 3           4) recognition of prior-period gains or losses (e.g., investment earnings
- 4           different from assumed or amortization of unrecognized gains and
- 5           losses); and
- 6           5) recognition of the cost of benefit changes the plan sponsor provides for
- 7           service the employees have already performed (amortization of
- 8           unrecognized prior service cost).

9

10 Q. TAKING EACH OF THESE FIVE COMPONENTS IN ORDER, HOW IS THE SERVICE  
11 COST COMPONENT CALCULATED?

12 A. The service cost component recognized in a period is the actuarial present  
13 value of benefits attributed by the pension benefit formula to current  
14 employees' service during that period. In effect, the service cost is the value  
15 of benefits that the employees have earned during the current period.  
16 Actuarial assumptions are used to reflect the time value of money (the  
17 discount rate) and the probability of payment (assumptions as to mortality,  
18 turnover, early retirement, and so forth).

19

20 Q. NEXT, HOW IS THE INTEREST COST COMPONENT CALCULATED?

21 A. The interest cost component recognized in a fiscal year is determined as the  
22 increase in the plan's total PBO due to the passage of time. Measuring the  
23 PBO as a present value requires accrual of an interest cost at a rate equal to  
24 the assumed discount rate. Essentially, the interest cost identifies the time  
25 value of money by recognizing that anticipated pension benefit payments are  
26 one year closer to being paid from the pension plan.

1 Q. HOW IS THE THIRD COMPONENT, EROA, CALCULATED?

2 A. The EROA is determined based on the expected long-term rate of return on  
3 the market value of plan assets. The market value of plan assets is a calculated  
4 value that recognizes changes in the fair value of assets in a systematic and  
5 rational manner over not more than five years. The EROA is an offset to the  
6 service costs and interest costs, and therefore it reduces the amount of  
7 pension expense.

8

9 Q. CAN YOU PROVIDE AN EXAMPLE OF HOW THE INVESTMENT EARNINGS  
10 REDUCE THE AMOUNT OF PENSION EXPENSE?

11 A. Yes. Assume that the pension trust fund has a beginning asset balance of  
12 \$500 million and the expected EROA in that year is 8 percent. The expected  
13 return is \$40 million (\$500 million x 8 percent). This amount will be used to  
14 offset the other components within the pension cost determination. Further  
15 assume that these other components are as follows: Service Cost (\$25 million),  
16 Interest Cost (\$20 million), and Loss Amortization (\$30 million). The net  
17 periodic pension cost for the year would be \$35 million as shown in Table 3:

18

**Table 3**

19

**Annual Pension Expense Example**

20

Amounts in Millions				
Service Cost	Interest Cost	Loss Amortization	EROA	Total
\$25	\$20	\$30	\$(40)	\$35

21

22

23

24

25

26

27

As shown in Table 3, the pension cost would have been \$75 million in the absence of the investment earnings. If the actual earned return in a particular year is higher than the EROA, customers will enjoy even more savings in future years as the asset gain is phased into pension expense.

1 Q. HAVE THE COMPANY'S CUSTOMERS EXPERIENCED THOSE TYPES OF SAVINGS  
2 IN PRIOR YEARS?

3 A. Yes. As I explained previously, the Company's annual pension cost included  
4 in rates has been significantly lower in prior years as a result of the earnings on  
5 the FAS 87 pension assets because those earnings helped reduce the amounts  
6 contributed by customers, relative to the true cost of the pension benefits.

7

8 Q. WITH REGARD TO THE FOURTH COMPONENT, WHAT ARE THE UNRECOGNIZED  
9 GAINS AND LOSSES?

10 A. The unrecognized gains and losses are the asset gains or losses and the liability  
11 gains or losses that I discussed earlier. The asset gains or losses occur because  
12 the actual earned return on assets was different from the EROA in prior years.  
13 The liability gains or losses occur because the actual values experienced in  
14 prior years, such as the discount rate and wage assumptions, were different  
15 from what was expected. The asset gains or losses are phased in according to  
16 the five-year schedule I discussed earlier, and then they are netted with not  
17 only the liability gains and losses from the previous year, but also the  
18 unamortized gains and losses from prior years. If the net unamortized gains  
19 or losses fall outside the ten-percent corridor, they are amortized over the  
20 remaining service lives of the Company's employees.

21

22 Q. PLEASE EXPLAIN IN MORE DETAIL THE PROCESS FOR DETERMINING WHETHER  
23 THE GAIN AND LOSS AMOUNT UNDER FAS 87 SHOULD BE AMORTIZED.

24 A. As noted in the decision tree that appears in Exhibit\_\_\_(RRS-1), Schedule 4,  
25 the determination of the gain or loss amortization is a multi-step process  
26 composed of the following steps:

- 1           1) The Company first determines whether it has an asset gain or loss by  
2           comparing the actual return on assets for the prior year to the EROA  
3           for the prior year.
- 4           2) To the extent there is an asset gain or a loss, the Company phases in 20  
5           percent of that gain or loss. The Company will also phase in portions  
6           of gains and losses from prior years that have not been fully phased in.  
7           They are phased in at the rate of 20 percent per year.
- 8           3) The Company then calculates the gain or loss on the PBO by  
9           comparing the actual year-end PBO from the prior year to the expected  
10          year-end PBO for the prior year.
- 11          4) The Company next aggregates the cumulative net gains and losses from  
12          all prior years to arrive at the cumulative unrecognized gains or losses.
- 13          5) If the cumulative unrecognized gains and losses are more than 10  
14          percent of the greater of the PBO or the market value of assets, the  
15          balance of gains and losses that falls outside the corridor is amortized  
16          over the average expected remaining years of service of the Company's  
17          employees.

18  
19 Q. IS THIS THE SAME PROCESS THAT THE COMPANY HAS FOLLOWED SINCE THE  
20 ORIGINATION OF THE XES PLAN?

21 A. Yes. The Company was required to set the phase-in period, as well as the  
22 basis for amortizing gains and losses at the time it adopted FAS 87, and it is  
23 not permitted to deviate from that basis from year to year.

24  
25 Q. WITH RESPECT TO THE FIFTH COMPONENT OF THE PENSION COST  
26 CALCULATION, WHAT IS UNRECOGNIZED PRIOR SERVICE COST?

1 A. Plan amendments can change benefits based on services rendered in prior  
2 periods. FAS 87 does not generally require the cost of providing such  
3 retroactive benefits (prior service cost) to be included in net periodic pension  
4 cost entirely in the year of the amendment, but instead provides for  
5 recognition over the future years.

6

7 Q. HOW IS UNRECOGNIZED PRIOR SERVICE COST AMORTIZED?

8 A. Unrecognized prior service cost is amortized over the expected remaining  
9 years of service of the participants impacted by the benefit change. Also,  
10 there is no ten-percent corridor for this purpose.

11

12 Q. HOW HAS THE COMPANY TREATED THE ASSET GAINS OF THE XES PLAN?

13 A. As noted earlier in connection with the NSPM Plan, all net asset gains have  
14 been used to reduce pension expense.

15

16 Q. DOES THE AMORTIZATION AMOUNT OF UNRECOGNIZED GAINS AND LOSSES  
17 REPRESENT THE ENTIRE FAS 87 EXPENSE?

18 A. No. As I discussed earlier, it is only one component of the FAS 87 pension  
19 expense. The service costs, interest costs, EROA and recognition of prior  
20 service costs are also components of the FAS 87 expense.

21

22 Q. YOU HAD MENTIONED PREVIOUSLY THAT A SIXTH COMPONENT OF PENSION  
23 COST CAN BE REQUIRED; WHAT IS THAT?

24 A. A sixth component, FAS 88 settlement accounting, can be required provided  
25 certain criteria are met during the year. Settlement accounting is required if  
26 lump-sum payments to employees in a year are greater than the sum of the  
27 service cost and interest cost components recognized for that year. This

1 criterion for settlement accounting was met in 2017 and 2018 for the XEPP.  
2 The XEPP's participant population has a significant proportion of participants  
3 at or nearing retirement age. The Company has seen significantly more lump-  
4 sum pension payouts in 2017 and 2018 than in years past, thus exposing the  
5 plan to settlement accounting requirements for the first time. When  
6 settlement accounting is triggered, the Company is immediately required to  
7 recognize a portion of unrealized losses currently deferred as a regulatory  
8 asset. When settlement accounting is not triggered, the unrecognized gain or  
9 loss is amortized over a much longer period of time.

10  
11 Q. DOES SETTLEMENT ACCOUNTING RESULT IN AN INCREASE IN THE OVERALL  
12 PENSION EXPENSE?

13 A. No. Settlement accounting is not an increase in the overall pension expenses,  
14 but rather an acceleration of the timing of when the pension expense will be  
15 recognized. Since the 2017 and 2018 FAS 88 settlement is part of the total  
16 recognized FAS 87 pension cost, it was factored into the cap and deferral  
17 mechanism for XES pension expense that was mentioned above. The  
18 deferred amount is described in more detail below.

19  
20 Q. DID THE XEPP FAS 88 SETTLEMENT ONLY AFFECT MINNESOTA CUSTOMERS?

21 A. No. One of the Company's other operating companies, Northern States  
22 Power Company Wisconsin (NSPW), also has employees in the XEPP. As a  
23 result, they were also subject to this provision, requiring them to also  
24 immediately recognize a portion of their unrealized losses as required by FAS  
25 88.

1 Q. HOW DID NSPW ADDRESS THE FAS 88 SETTLEMENT CHARGE?

2 A. NSPW requested deferred accounting treatment for the 2017 and 2018  
3 pension settlement charges, which was granted. NSPW also received approval  
4 to amortized and include the deferred balances in 2020 rates, Interim Order  
5 4220-UR-124.

6

7 Q. DOES THE ACM ALSO HAVE A SETTLEMENT ACCOUNTING PROVISION?

8 A. No, the ACM does not have a settlement accounting provision.

9

10 **E. Pension Funding**

11 Q. DO THE ACM AND FAS 87 ALSO GOVERN HOW RETIREMENT PLANS MUST BE  
12 FUNDED?

13 A. No. The funding of retirement plans is determined based upon prudent  
14 business practices as limited by the provisions of the Employee Retirement  
15 Income Security Act (ERISA), the Pension Protection Act, and the Internal  
16 Revenue Code (IRC). Under those laws and regulations:

- 17
- 18 • There are minimum required contributions;
  - 19 • There are maximum contributions that can be deducted for tax  
20 purposes; and
  - 21 • The plan sponsor has a fiduciary responsibility to prudently protect the  
22 interests of the plan participants and beneficiaries.

22 Over the long run, the cumulative employer contributions made to a plan in  
23 accordance with ERISA, the Pension Protection Act, and the IRC rules will  
24 be roughly equal to the cumulative pension expense recorded under both the  
25 ACM and FAS 87; but in the short and intermediate run, there can be  
26 significant differences. The cumulative difference between pension  
27 contributions and recognized pension expense gives rise to a prepaid pension

1 asset or a pension liability, both of which I will explain in greater detail later in  
2 my testimony.

3  
4 **IV. PENSION ASSUMPTIONS**

5  
6 Q. PLEASE SUMMARIZE THE THREE PRIMARY PENSION ASSUMPTIONS USED TO  
7 DETERMINE THE MULTI-YEAR RATE PLAN PENSION COST.

8 A. The primary pension assumptions used to determine the multi-year rate plan  
9 pension costs are the discount rate and the EROA. The Company used the  
10 following assumptions in Table 4 to determine 2020-2022 pension expense:

11 **Table 4**  
12 **2020-2022 Pension Assumptions**

13

<b>Company – Accounting Method</b>	<b>Discount Rate</b>	<b>EROA</b>
NSPM – Aggregate Cost Method (ACM)	7.10%	7.10%
XES – FAS 87 (ASC 715)	4.15%	7.10%

14  
15  
16

17 Q. HAS THE COMPANY PROVIDED OBJECTIVE, VERIFIABLE MEASURES TO  
18 EVALUATE THE ASSUMPTIONS?

19 A. We have provided objective, verifiable measures where they are available. For  
20 example, we used Citigroup benchmark indexes to evaluate the reasonableness  
21 of the discount rate produced by our bond-matching study, which we used in  
22 determining the Company’s five-year average discount rate. For the EROA  
23 assumptions, we gathered information from the 2018 Edison Electric Institute  
24 (EEI) survey results for fiscal year 2018, and we compared those other  
25 utilities’ assumptions to ours. The results are shown on Exhibit\_\_\_\_(RRS-1),  
26 Schedule 7.

1 Q. WHAT DOES THE COMPARISON SHOW?

2 A. The EROA and wage increase assumptions used for the NSPM Plan and the  
3 XES Plan are at or near the average of the 47 EEI companies who responded  
4 to the survey.

5

6 1) The NSPM Plan discount rate of 7.10 percent is much higher than the  
7 average discount rate of 4.31 percent for the 47 EEI companies who  
8 responded to the survey. This is due to the ACM requirement that the  
9 discount rate be set equal to the EROA, a requirement not faced by any  
10 company not using ACM. A higher discount rate assumption lowers  
11 the cost, so the NSPM discount rate assumption lowers cost as  
12 compared to other utilities, all else equal.

13

14 2) Regarding the XES Plan discount rate, as I noted earlier in my  
15 testimony, the Company continues to believe that the correct method  
16 to arrive at the FAS 87 discount rate is by performing a bond-matching  
17 study for a single year. However, we have used a five-year average  
18 discount rate in this case, consistent with prior Commission orders, to  
19 reduce the number of contested issues and to allow the parties to focus  
20 instead on the Company's proposed multi-year rate plan. The XES  
21 FAS 87 five-year average discount rate is 4.15 percent, compared to the  
22 EEI survey average of 4.31 percent.

23

24 3) The NSPM Plan and the XES Plan EROA assumptions of 7.10 percent  
25 are slightly higher than the 7.00 percent average for the EEI companies.  
26 The Company's slightly higher EROA also decreases costs, as  
27 compared to the 7.00 average.



1 A. The Company uses multiple reference points to set the discount rate. The  
2 primary basis for valuation is a bond-matching study that is performed as of  
3 December 31 of each year. The bond-matching study selects a matching bond  
4 for each of the individual projected payout durations within the plan based on  
5 projected actuarial experience, as compiled by the Company's actuary, Willis  
6 Towers Watson. The bonds selected must have a rating of Aa/AA or higher  
7 and not have a pending review as of December 31. In addition, the bond may  
8 not have an inconsistent rating between agencies where any agency rates the  
9 bonds below Aa/AA. If bonds are not available for a specific duration within  
10 the plan, a bond with the next closest shorter duration is used to determine  
11 the discount rate. The Company currently uses a single, average discount rate  
12 for all pension plans because the individual plans have a materially consistent  
13 duration and cash flow pattern. Individual discount rates by plan are  
14 identified and reviewed for significant deviations from the average in the  
15 determination of the overall rate.

16  
17 The Company also uses other reference points to validate the rate calculated  
18 by the bond-matching study, including the Citigroup Benchmark and the  
19 Citigroup Above Median Benchmark. In addition to these reference points,  
20 the Company also reviews general survey data provided by Willis Towers  
21 Watson and EEI to assess the reasonableness of the discount rate selected.

22  
23 The Company has consistently used the bond-matching approach, along with  
24 the corroborating methods, because it provides the most accurate discount  
25 rate of the available alternatives that meet applicable standards of FAS 87.  
26 Further information pertaining to the determination of discount rates is  
27 provided in Exhibit\_\_\_\_(RRS-1), Schedule 8. These standards and the review

1 processes described below support the use of the discount rates used in  
2 determining the five-year average discount rate above that is used to determine  
3 pension expense for the XES Plan.  
4

5 Q. DESCRIBE THE FINANCIAL VALIDATION PROCESS AND CONTROLS THAT ARE IN  
6 PLACE REGARDING SETTING THE DISCOUNT RATE.

7 A. The Company has a Pension Trust Administration Committee (PTAC).  
8 Preliminary discount rates are reviewed by the PTAC in late December with  
9 potential year-end scenarios. Because discount rates are not set until the  
10 December 31 rates are available, the review at the initial meeting is primarily to  
11 set expectations. Year-end discount rates are developed using a bond-  
12 matching study applied to projections of future cash outflows for benefit  
13 payments, as I described earlier. Bond-matching study results are reviewed  
14 jointly with the Company Controller, the director in charge of benefits  
15 accounting, and representatives from Willis Towers Watson. Each individual  
16 bond is analyzed to consider any attributes that would make it inappropriate  
17 for the bond-matching study. This includes any known risk of downgrade to  
18 the bond, any deviation in yield from other bonds of the same duration, and  
19 the total outstanding and traded value of the bond. The results of the study  
20 are compared to publicly available sources such as the Citigroup Pension  
21 Liability Index and Citigroup Pension Curve to validate the reasonableness of  
22 the discount rate determined using the bond-matching study. Any unusual  
23 deviations between these numbers are researched to understand the  
24 underlying drivers.

25  
26 Bonds selected in the bond-matching study are revalidated by Willis Towers  
27 Watson prior to filing the Company's 10-K to ensure that individual bonds

1 selected have not been downgraded or put on watch. In addition, employee  
2 data used to determine the projected future payments is compared to previous  
3 years for reasonableness of the headcount and pay rate information, both  
4 internally and by Willis Towers Watson. Final discount rates are  
5 communicated back to the PTAC for approval, and the final approved rate is  
6 included in the meeting minutes. Final approved discount rate assumptions  
7 are then provided to the audit committee as part of the Company's critical  
8 accounting policies.

9  
10 In addition to the year-end discount rate analysis, discount rates are regularly  
11 recalculated over the course of the year by Pacific Global Advisors (PGA),  
12 Willis Towers Watson, and independently by Company personnel using  
13 projected cash flows combined with publicly published Citigroup Pension  
14 Liability Curve rates to understand the expected impact of changing rates as  
15 market conditions change. Changes in the 10-year Treasury rate and the  
16 Citigroup Pension Liability Index are used as indicators that pension discount  
17 rates are likely deviating from current assumptions and will often drive  
18 incremental estimates of expected discount rates.

19  
20 Q. HOW WAS THE 7.10 PERCENT NSPM PLAN DISCOUNT RATE DETERMINED?

21 A. Pension expense for the NSPM Plan is based on the ACM, which requires use  
22 of the long-term EROA as the discount rate. Thus, the determination of the  
23 appropriate level of EROA, which is discussed below, also addresses the  
24 appropriateness of the ACM discount rate.

25  
26 Q. WHAT IS YOUR CONCLUSION REGARDING THE DISCOUNT RATES USED FOR THE  
27 XES PLAN AND THE NSPM PLAN?

1 A. The test year discount rates for the XES Plan of 4.15 percent and the NSPM  
2 Plan of 7.10 percent are reasonable and in the case of NSPM Plan are well  
3 above the average rates used by other companies. As I have indicated, the  
4 Company does not necessarily agree with the use of a five-year average, but  
5 we are proposing it in this case, consistent with the Commission's decision in  
6 our 2013 rate case, to reduce the number of contested issues, which will help  
7 the parties focus on evaluating the merits of our multi-year proposal.

8

9 Q. WILL THE COMPANY UPDATE ITS PROPOSED DISCOUNT RATE?

10 A. Yes. Consistent with the past practice, the Company will recalculate its test  
11 year pension cost using a measurement date of December 31, 2019, to capture  
12 the most current pension position and to provide an update to all elements of  
13 cost.

14

15 **B. EROA Assumption**

16 Q. WHAT IS THE TEST YEAR EROA?

17 A. The test year EROA is 7.10 percent. In the Company's 2015 rate case, the  
18 Company's EROA assumption was 7.25 percent.

19

20 Q. WHY DID THE COMPANY LOWER THE EROA ASSUMPTION?

21 A. The Company decreased the EROA assumption primarily because the interest  
22 rates on fixed-income securities have continued to fall, which reduces the  
23 expected return on those assets.

24

25 Q. HOW WAS THE TEST YEAR EROA ASSUMPTION DETERMINED?

26 A. The EROA is, and must be, determined based on the long-term expected rates  
27 of return as dictated by the requirements of the ACM and FAS 87. The

1 Company bases investment return assumptions on expected long-term  
2 performance for each of the investment types included in our pension asset  
3 portfolio – equity investments (such as corporate common stocks), fixed-  
4 income investments (such as corporate bonds and U.S. Treasury securities),  
5 and alternative investments (such as private equity, hedge fund-of-funds,  
6 commodities, or real estate partnerships). In reaching return assumptions, the  
7 Company considers the actual historical returns achieved, as well as the long-  
8 term return levels projected and recommended by investment experts in the  
9 marketplace. Xcel Energy continually reviews its pension investment  
10 assumptions in order to maintain investment portfolios that provide adequate  
11 rates of return at appropriate levels of risk. Further information pertaining to  
12 the determination of EROA is provided in Exhibit\_\_\_(RRS-1), Schedule 8.

13  
14 Q. DESCRIBE THE FINANCIAL VALIDATION PROCESS AND CONTROLS THAT ARE IN  
15 PLACE REGARDING SETTING THE EROA ASSUMPTION.

16 A. The PTAC develops and validates rate-of-return assumptions jointly with  
17 Goldman Sachs, which is the Company's external pension investment advisor.  
18 With the help of Goldman Sachs, the Company's treasury group establishes a  
19 target investment strategy and investment mix. This investment strategy and  
20 mix are then presented at the PTAC meeting for approval. The target  
21 portfolio investment mix is then matched with expected long-term returns  
22 provided by Goldman Sachs for each of the investment classes within the  
23 portfolio. The expected long-term returns are validated against other advisor  
24 group benchmarks and expected returns by asset class provided by Willis  
25 Towers Watson. The results of these weighted average investment returns are  
26 aggregated to arrive at a single average long-term rate of return by plan that is  
27 then included in the assumptions provided to the PTAC for review, and they

1 are included in the Company's critical accounting policies provided to the  
2 audit committee.

3  
4 Q. DOES THE COMPANY COMPARE ITS EROA TO OTHER COMPANIES?

5 A. Yes. The Company compares its EROA to other utilities and also to general  
6 industry data. Exhibit\_\_\_(RRS-1), Schedule 7 shows that the Company's  
7 long-term EROA assumption of 7.10 percent is slightly higher than the  
8 average of 7.00 percent for the EEI utilities.

9  
10 Q. WHAT IS YOUR CONCLUSION REGARDING THE 7.10 PERCENT EROA?

11 A. The 7.10 percent EROA assumption is reasonable based on the requirement  
12 that the return be based on the target investment mix of the Company's  
13 pension plan assets. Mr. Inglis discusses the reasonableness of the Company's  
14 target asset allocation and investment strategy in more detail in his testimony.

15  
16 **V. QUALIFIED PENSION AND 401(K) MATCH COSTS**

17  
18 Q. WHAT DO YOU DISCUSS IN THIS SECTION OF YOUR TESTIMONY?

19 A. I quantify the multi-year rate plan expense amounts for qualified pension and  
20 401(k) match.

21  
22 **A. Qualified Pension Expense**

23 Q. WHAT IS THE LEVEL OF QUALIFIED PENSION EXPENSE IN EACH YEAR OF THE  
24 MULTI-YEAR RATE PLAN?

25 A. The 2020, 2021, and 2022 qualified pension expense amounts are  
26 approximately \$21.0 million, \$20.4 million, and \$19.8 million, respectively.  
27 These amounts include costs related to both the NSPM Plan and the XES

1 Plan. Approximately 75 percent of the Company's qualified pension expense  
2 relates to the NSPM Plan and 25 percent relates to the XES Plan.

3  
4 Q. DO THE NSPM PLAN AND THE XES PLAN DETERMINE THEIR QUALIFIED  
5 PENSION EXPENSE USING DIFFERENT METHODS?

6 A. Yes. As I indicated in an earlier section of my testimony, the ACM continues  
7 to be used to determine the expense of the NSPM Plan. Thus, the pension  
8 expense for that plan consists of a levelized percentage of payroll that is  
9 sufficient to recover the current year's portion of the difference between the  
10 PVFB and the asset value. In contrast, costs of the XES Plan costs are  
11 established based on the five elements prescribed by FAS 87 – service cost,  
12 interest cost, the EROA, unrecognized gains or losses, and unrecognized prior  
13 service costs.

14  
15 Q. ARE THE TWO METHODS BASED ON ANY COMMON ASSUMPTIONS?

16 A. Yes. To calculate the pension liability under both methods, it is necessary to  
17 make assumptions about the discount rate and demographics (including  
18 attrition, expected wage increases, etc.) The assumptions are established at the  
19 end of each year, and they are used to determine book expense for the  
20 subsequent year. Accordingly, the 2019 assumptions were finalized as of  
21 December 31, 2018, and the 2020 assumptions will be finalized as of  
22 December 31, 2019. The final 2020 assumptions will be available in late  
23 January 2020. The Company has typically included updated cost amounts in  
24 Rebuttal Testimony. We also recognize that our updates should be objectively  
25 validated when possible, and we will provide the available validation measures  
26 in both this testimony and my Rebuttal Testimony. I provided detailed

1 support for each of the two major pension assumptions in the prior section of  
2 my testimony.

3  
4 Q. WHAT WERE THE AMOUNTS OF QUALIFIED PENSION EXPENSE IN THE FIVE  
5 YEARS PRIOR TO THE TEST YEAR, AND WHAT DOES THE COMPANY EXPECT  
6 THEM TO BE OVER THE NEXT FEW YEARS?

7 A. Table 6 below shows pension expense amounts since 2015 and the Company's  
8 current forecast of qualified pension expense. The forecast for 2019 and  
9 beyond assumes no changes in assumptions for the EROA, discount rate, plan  
10 contributions, wage increases, and employee turnover. The forecast also  
11 assumes that actual experience matches these assumptions, including the  
12 Company's actual return on assets equaling the EROA in 2019 and all  
13 subsequent years. Additionally, where applicable, the amounts reflect the  
14 impacts of pension expense being calculated using a five-year average discount  
15 rate and applying the two additional mitigation methods that the Commission  
16 accepted in Docket No. E002/GR-12-961, including the proposed change to  
17 the XES cap discussed below.

18 **Table 6**  
19 **Qualified Pension Expense**

20

NSPM Electric O&M State of MN	
Year	Amount (\$)
2015	19,845,733
2016	18,815,654
2017	21,398,738
2018	20,549,083
2019 Forecast	21,427,184
2020 Test Year	20,956,503
2021 Plan Year	20,378,317
2022 Plan Year	19,780,720

21  
22  
23  
24  
25  
26  
27

1 Q. WHAT ARE THE MAJOR DRIVERS OF THE DECREASE IN QUALIFIED PENSION  
2 EXPENSE?

3 A. The major drivers of the changes in qualified pension expense are:

- 4 • a decrease in the asset loss amortization;
- 5 • improved funded status from contributions and expected return on  
6 assets; and
- 7 • plan design changes.

8

9 Q. PLEASE DISCUSS THE RECENT DECREASE IN THE ASSET LOSS AMORTIZATION,  
10 AND EXPLAIN HOW THIS CONTRIBUTES TO THE DECREASE IN PENSION  
11 EXPENSE.

12 A. The asset loss amortization was explained in detail in Section III. Also, see  
13 Exhibit\_\_\_(RRS-1), Schedule 3, which shows the declining loss amounts in  
14 the 2020-2022 multi-year rate plan.

15

16 Q. PLEASE DESCRIBE HOW CONTRIBUTIONS AND THE EXPECTED RETURN ON  
17 ASSETS CONTRIBUTES TO THE DECREASE IN PENSION EXPENSE.

18 A. Because of funding requirements mandated by the Pension Protection Act of  
19 2006, the Company has made significant contributions to the pension trust  
20 funds in recent years. Those contributions increase the assets upon which the  
21 Company earns a return, and those returns are an offset to annual pension  
22 cost. Thus, the increase in the asset base helps to reduce annual pension cost.

23

24 Q. PLEASE DISCUSS HOW PENSION PLAN DESIGN CHANGES CONTRIBUTE TO THE  
25 DECREASE IN PENSION EXPENSE.

26 A. Plan design changes implemented in 2011 and 2012 significantly reduced  
27 benefit levels for newly hired bargaining and non-bargaining employees. Each

1 year as new employees are hired, the Company will continue to see increased  
2 savings as new employees are enrolled in the revised pension benefit plan. In  
3 addition, effective on January 1, 2018, the annual RSA credits were eliminated  
4 on a going-forward basis for all non-bargaining employees and the Social  
5 Security Supplement was eliminated for all non-bargaining employees who will  
6 not meet certain criteria, including retirement eligibility, by December 31,  
7 2022. The Company has estimated that these changes have reduced qualified  
8 pension expense by at least \$5 to \$6 million each year over the multi-year rate  
9 plan.

10  
11 Q. HAS THE COMPANY PROVIDED THE ACTUARIAL STUDY AND DERIVATION OF  
12 THE JURISDICTIONAL AMOUNT?

13 A. Yes. The Company has included Exhibit\_\_\_(RRS-1), Schedule 9, which is an  
14 actuarial study that supports the qualified pension costs included in the multi-  
15 year rate plan. Exhibit\_\_\_(RRS-1), Schedule 10 shows the conversion of the  
16 2020 total cost amounts to the NSPM electric O&M, state of Minnesota  
17 amount.

18  
19 **B. 401(k) Match**

20 Q. WHAT IS THE 401(K) MATCH EXPENSE AMOUNT IN EACH YEAR OF THE MULTI-  
21 YEAR RATE PLAN?

22 A. The 2020, 2021, and 2022 401(k) match expense amounts are approximately  
23 \$9.3 million, \$9.6 million, and \$9.8 million, respectively.

24  
25 Q. WHAT WERE THE AMOUNTS OF 401(K) MATCH EXPENSES IN THE FIVE YEARS  
26 PRIOR TO THE TEST YEAR COMPARED TO THE FORECASTED AMOUNTS FOR THE  
27 MULTI-YEAR RATE PLAN PERIOD?

1 A. Table 7 below shows the amounts of 401(k) match expense from 2015  
2 through 2019.

3 **Table 7**  
4 **401(k) Match Expense**

5

NSPM Electric O&M State of MN	
<b>Year</b>	<b>Amount (\$)</b>
2015	9,125,327
2016	9,194,646
2017	8,886,008
2018	9,036,008
2019 Forecast	9,259,666
2020 Test Year	9,313,718
2021 Plan Year	9,553,390
2022 Plan Year	9,809,095

6  
7  
8  
9  
10  
11  
12  
13

14  
15 Q. WHAT ASSUMPTIONS WERE USED TO DEVELOP THE 401(K) MATCH EXPENSE  
16 FOR 2020-2022?

17 A. The most recent actual 401(k) match, which was from the 2018 plan year, was  
18 used as the base year. This base year amount was then increased by the 2019  
19 estimated and 2020-2022 budgeted merit increases to derive the amounts in  
20 2020-2022.

21  
22 Q. WHY IS THE AMOUNT OF 401(K) EXPENSE INCREASING EACH YEAR?

23 A. The 401(k) expense is increasing because the contribution is calculated based  
24 on a percentage of salary; and merit salary increases cause the total labor costs  
25 to increase each year. Moreover, the Company has experienced an overall  
26 increase in 401(k) participation in recent years, and that trend is expected to  
27 continue.

1           **C.     Qualified Pension Deferred Balances**

2    Q.   WHAT RECENT ACTIONS HAVE IMPACTED THE COMPANY’S RECOVERY  
3        QUALIFIED PENSION COSTS?

4    A.   In the 2013 electric rate case Docket No. E002/GR-12-961, the Company  
5        introduced, and the Commission approved, two alternative cost recovery  
6        methods for its qualified pension costs – a twenty year amortization period for  
7        unrecognized pension costs for the NSPM Plan and a “cap and defer”  
8        recovery of XES pension costs. In Docket No. E002/GR-13-868, the  
9        Commission approved the continuation of those methods, stating:

10           The Commission will adopt the ALJ’s recommendation to  
11           require continuation of the qualified pension mitigation  
12           approved in the Company’s 2012 rate case. As the ALJ  
13           recognized, this mitigation method has previously been found  
14           to be consistent with the public and ratepayer interests, and this  
15           record supports the same conclusion. The Commission will  
16           therefore again require the Company to extend the NSPM Plan  
17           amortization period for unrecognized pension costs from 10 to  
18           20 years; and cap the XES pension expense at the 2011 level of  
19           \$6.1 million and defer any excess of this amount to future  
20           years.  
21

22   Q.   IS THE COMPANY PROPOSING TO CONTINUE THESE TWO PROPOSALS IN THIS  
23        CASE?

24   A.   Yes. The qualified pension amounts included in this rate case have been  
25        adjusted for the extension of the amortization period from 10 to 20 years and  
26        the XES pension cap that was previously approved by the Commission in the  
27        Company's 2012 rate case.

28  
29   Q.   WHAT IS THE IMPACT FROM THESE TWO CHANGES ON 2020 QUALIFIED  
30        PENSION EXPENSE?

1 A. These two changes have reduced the test year qualified pension expense by  
2 \$1,623,362.

3

4 Q. HOW WOULD YOU CHARACTERIZE THE DEFERRED AMOUNTS?

5 A. These deferred amounts represent shareholder funds that the Company will  
6 not recover until a future time period, or a prepayment. The general  
7 ratemaking practice is for a utility prepayment to be added to rate base and for  
8 a customer prepayment to be subtracted from rate base.

9

10 Q. SO IS THE COMPANY EARNING A RETURN ON THE AMOUNTS DEFERRED TO  
11 FUTURE YEARS?

12 A. No. Although such treatment of these funds would be appropriate in order to  
13 make shareholders whole, in Docket No. E002/GR-13-868, the Commission  
14 stated that the deferred amounts “will not be included in rate base.”  
15 Consistent with this Order, the Company has not earned a return on these  
16 deferrals, and in order to minimize contested issues in this proceeding, we  
17 have not included the deferred amounts in rate base in this proceeding either.

18

19 Q. DID THE COMMISSION PROVIDE ANY OTHER GUIDANCE WITH RESPECT TO THE  
20 DEFERRED BALANCE IN DOCKET NO. E002/GR-13-868?

21 A. Yes. On page 20 of the Docket No. E002/GR-13-868 Order, the  
22 Commission directed that, “if approved recovery exceeds future years’  
23 pension expense, the Company will apply that amount to recovery of the  
24 deferred XES pension expense amounts.” The Commission also stated, “The  
25 Company shall file annual compliance reports which provide its pension plans’  
26 cost-calculation reports, the XES Plan accumulated deferred balance, and the  
27 excess rate-level recovery applied toward satisfying the deferral.”

1 Q. HAS THE COMPANY CREATED THE REQUIRED ANNUAL COMPLIANCE FILING  
2 WHICH INCLUDES THE DEFERRED PENSION BALANCES?

3 A. Yes. Exhibit\_\_\_(RRS-1), Schedule 11 provides the requested annual  
4 compliance filing, which shows how the deferred amount was built up and  
5 how it is expected to unwind over the course of the multi-year plan.

6

7 Q. DOES THE COMPANY HAVE ANY OTHER REQUESTS RELATED TO THESE  
8 DEFERRED BALANCES?

9 A. Yes. The Company proposes to amortize the December 31, 2018 XES Plan  
10 cap cumulative deferred balance of \$17,644,894 over the three years of the  
11 multi-year plan, or \$5,881,632 per year. Company witnesses Mr. Chamberlain  
12 and Mr. Halama discuss the appropriateness of the three-year amortization  
13 period. The history of the cumulative deferred balance can be found in  
14 Exhibit\_\_\_(RRS-1), Schedule 11, on the Sch B-XES, Page 2. For further  
15 discussion around these deferred balances, including a description of the FAS  
16 88 settlement, see the Company's response to Information Request (IR)  
17 DOC-2163 and DOC-2164 in Docket No. E002/GR-15-826 and can be  
18 found in Exhibit\_\_\_(RRS-1), Schedule 12.

19

20 **D. Qualified Pension and 401(k) Match Benefits Summary**

21 Q. PLEASE SUMMARIZE THE COMPANY'S REQUEST REGARDING THE MULTI-YEAR  
22 RATE PLAN AMOUNTS FOR THESE TWO BENEFITS.

23 A. The Company requests that the Commission approve the 2020, 2021, and  
24 2022 qualified pension expense amounts of \$20,956,503, \$20,378,317, and  
25 \$19,780,720 and 401(k) match expense amounts of \$9,313,718, \$9,553,390,  
26 and \$9,809,095 respectively. The qualified pension expense amounts include  
27 continuing the two normalization methods previously approved and updating

1 the XES Plan cap to the 2019 qualified pension forecasted amount of  
2 \$5,055,526. Finally, the Company requests to amortize the December 31,  
3 2018 cumulative deferred balance related to XES cap of \$17,379,449 over the  
4 three years of the multi-year rate plan.

5  
6 Q. IS IT REASONABLE TO ASK CUSTOMERS TO PAY FOR QUALIFIED PENSION AND  
7 401(K) MATCH BENEFIT COSTS?

8 A. Yes. It is appropriate that customers pay for these benefits because they  
9 reflect a reasonable and necessary level of expense. As explained in more  
10 detail in the testimony of Ms. Lowenthal, our compensation and benefits plans  
11 are required to attract, retain, and motivate employees needed to perform the  
12 work necessary to provide quality services for NSPM customers. Without the  
13 qualified pension plan and 401(k) matching benefits, the Company would have  
14 to pay significantly higher current compensation to attract employees.

15  
16 **VI. RETIREE MEDICAL AND FAS 112 LONG-TERM**  
17 **DISABILITY BENEFITS**

18  
19 Q. WHAT DO YOU DISCUSS IN THIS SECTION OF YOUR TESTIMONY?

20 A. I discuss the Company's request to recover the expense for post-retirement  
21 healthcare benefits under FAS 106, Employers' Accounting for Post-  
22 Retirement Benefits Other Than Pensions and for post-employment long-  
23 term disability (LTD) benefits under FAS 112, Employers' Accounting for  
24 Post-Employment Benefits.

25  
26 Q. PLEASE EXPLAIN THE DIFFERENCE BETWEEN FAS 106 AND FAS 112 LTD  
27 BENEFITS.

1 A. The FAS 106 benefits are primarily post-retirement healthcare benefits. FAS  
2 112 encompasses a number of benefits, including LTD, workers'  
3 compensation, and continuation of life insurance.

4  
5 **A. Retiree Medical**

6 Q. DOES THE COMPANY STILL OFFER FAS 106 RETIREE MEDICAL BENEFITS TO ITS  
7 ACTIVE EMPLOYEES?

8 A. No. The Company eliminated FAS 106 retiree medical benefits for all active  
9 non-bargaining and bargaining employees more than ten years ago. The  
10 current expense for retiree medical benefits is a legacy of the prior programs.

11  
12 Q. PLEASE EXPLAIN HOW RETIREE MEDICAL COSTS ARE DETERMINED.

13 A. The components and calculation of FAS 106 are identical to FAS 87, with one  
14 exception. Unlike FAS 87, FAS 106 asset gains or losses are not phased in  
15 before they are amortized; but instead, the total gain or loss amount is simply  
16 amortized over the average years to retirement for active employees.  
17 Otherwise, the FAS 106 benefits are calculated based on assumptions  
18 regarding the discount rate, the EROA, and the salary or wage levels.

19  
20 Q. WHAT ARE THE ASSUMPTIONS REGARDING THE DISCOUNT RATE AND THE  
21 EROA FOR THE MULTI-YEAR RATE PERIOD?

22 A. The 2020-2022 multi-year rate period reflects an EROA of 5.30 percent for  
23 both bargaining and non-bargaining employees. It reflects a 4.16 percent  
24 discount rate, which is the five-year average discount rate.

1 Q. PLEASE DESCRIBE HOW THE 4.16 PERCENT DISCOUNT RATE WAS DETERMINED  
2 FOR THIS RATE CASE.

3 A. The Company determined the 4.16 percent discount rate consistent with  
4 qualified pension. Table 8 below supports how the five-year average discount  
5 rate of 4.16 was determined.

6 **Table 8**  
7 **FAS 106 Retiree Medical Discount Rate**

8

Current Rate Case - Using Historical Actuals						
Expense Period	2015	2016	2017	2018	2019	Average
Measurement Date	12/31/2014	12/3/2015	12/31/2016	12/31/2017	12/31/2018	5-Year
Discount Rate	4.08%	4.65%	4.13%	3.62%	4.32%	4.16%

9  
10  
11  
12

13

14 Q. WILL THE COMPANY PROVIDE AN UPDATED FIVE-YEAR AVERAGE DISCOUNT  
15 RATE TO INCORPORATE THE MOST RECENT MEASUREMENT DATE?

16 A. Yes. As we have done in prior rate cases, the Company will provide an  
17 updated five-year average discount rate in Rebuttal Testimony to incorporate  
18 the most recent measurement date of December 31, 2019, which will be  
19 available in late January or early February of 2020.

20 Q. PLEASE DESCRIBE HOW THE DISCOUNT RATES LISTED ABOVE IN TABLE 8 FOR  
21 THE FIVE-YEAR AVERAGE DISCOUNT RATE WERE DETERMINED.

22 A. The process for determining the discount rate for retiree medical is the same  
23 as for pension and is built from the same portfolio of bonds developed  
24 through the Company's bond-matching study. This common set of bonds is  
25 then applied to the plan-specific cash flows to arrive at a weighted average  
26 discount rate appropriate for each individual plan. The EROA assumption is  
27 based on the expected long-term performance for each of the investment

1 types included in its post-retirement healthcare asset portfolio. Because the  
2 post-retirement medical benefits are generally payable on a shorter time  
3 horizon than the qualified pension expense benefits are, the Company uses  
4 shorter duration investments for the post-retirement medical benefit expense,  
5 which lowers the EROA somewhat.

6  
7 Q. WHAT WERE THE AMOUNTS OF FAS 106 RETIREE MEDICAL EXPENSE IN THE  
8 FIVE YEARS PRIOR TO THE TEST YEAR, AND WHAT DOES THE COMPANY EXPECT  
9 THEM TO BE OVER THE NEXT FEW YEARS?

10 A. As Table 9 below shows, the test year retiree medical costs are the lowest they  
11 have been over this time period. This decrease in retiree medical costs has  
12 been the norm over the last several years and is primarily due to the fact that,  
13 as time passes, fewer employees are eligible for the benefit because it was  
14 closed to new participants more than a decade ago. Because of the foregoing  
15 factors, the FAS 106 expenses have decreased despite lower discount rates and  
16 the amortization of net gains and losses, both of which had the effect of  
17 increasing costs. Additionally, the Company implemented plan changes in  
18 2013 to transition Medicare-eligible retirees and dependents to a healthcare  
19 exchange, which has also reduced costs.

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26

**Table 9**

**FAS 106 Retiree Medical Expense**

NSPM Electric O&M State of MN	
Year	Amount (\$)
2015	2,118,910
2016	1,612,940
2017	1,511,399
2018	1,458,735
2019 Forecast	1,103,990
2020 Test Year	1,266,780
2021 Plan Year	1,138,526
2022 Plan Year	1,040,350

Q. HAS THE COMPANY PROVIDED THE ACTUARIAL STUDY AND DERIVATION OF THE JURISDICTIONAL AMOUNT?

A. Yes. The Company has included Exhibit\_\_\_(RRS-1), Schedule 9, which is an actuarial study that supports the FAS 106 costs for 2020-2022. Exhibit\_\_\_(RRS-1), Schedule 10 shows the conversion of the 2020 total cost amounts to the NSPM electric O&M, state of Minnesota amount.

**B. FAS 112 Long-Term Disability Benefits**

Q. PLEASE DESCRIBE FAS 112 LONG-TERM DISABILITY BENEFITS, AND EXPLAIN HOW THEY ARE ACCOUNTED FOR.

A. LTD benefits are provided by the Company to former or inactive employees after employment but before retirement. The LTD plan provides the employee income protection by paying a portion of the employee's income while he or she is disabled by a covered physical or mental impairment.

1 The accounting treatment varies depending on whether the cost is self-insured  
2 or fully-insured. In a fully-insured plan, the Company purchases an insurance  
3 plan from an outside insurance provider that assumes the risk. In a self-  
4 insured plan, the Company provides the benefits to the covered individuals  
5 and therefore, effectively acts as the insurer. For the self-insured piece, the  
6 Company is required to accrue for LTD costs under FAS 112, while the fully-  
7 insured piece is simply the cost of the insurance premium incurred each year  
8 along with any other miscellaneous costs. The FAS 112 accrual represents the  
9 expected disability benefit payments for employees that are not expected to  
10 return to work.

11  
12 Q. WHAT GROUPS OF EMPLOYEES ARE COVERED UNDER THE SELF-INSURED  
13 BENEFIT AND WHICH GROUPS ARE COVERED UNDER THE FULLY INSURED  
14 BENEFIT?

15 A. All non-bargaining employees disabled prior to January 1, 2008 and NSP  
16 bargaining employees disabled prior to January 1, 2014 are covered under the  
17 self-insured plan; and all employees disabled after these dates are covered  
18 under a fully insured plan.

19  
20 Q. WHAT WERE THE AMOUNTS OF FAS 112 LONG-TERM DISABILITY EXPENSE IN  
21 THE FIVE YEARS PRIOR TO THE TEST YEAR, AND WHAT DOES THE COMPANY  
22 EXPECT THEM TO BE OVER THE NEXT FEW YEARS?

23 A. Table 10 below compares the FAS 112 long-term disability benefit costs from  
24 2015 through 2022.

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26

**Table 10**

**FAS 112 Long-Term Disability Expense**

<b>NSPM Electric O&amp;M State of MN</b>	
<b>Year</b>	<b>Amount (\$)</b>
2015	678,459
2016	(490,613)
2017	62,298
2018	11,661
2019 Forecast	(73,979)
2020 Test Year	110,266
2021 Plan Year	102,611
2022 Plan Year	96,468

Q. WHAT CAUSES THE FLUCTUATIONS IN THESE COSTS FROM YEAR TO YEAR?

A. The FAS 112 self-insured costs fluctuate from year to year because of changes to the discount rate or demographic adjustments, such as changes in the number of disabled employees or changes in the amount of the average monthly disability benefit. Discount rate changes and demographic adjustments are the differences between actual experience and assumed experience and are recorded in the current year, which can result in significant changes in costs from one year to the next. The cost change was significant because, unlike pension, there is no amortization for gains and losses since there are no active employees to accrue the gain or loss over. Instead, the entire amount is recorded when it is determined. The cost then increased in 2020 because we have assumed no further changes to the discount rate. It is reasonable to assume no further changes to the FAS 112 discount rate as our assumptions are the most reasonable estimate to determine 2020 to 2022 costs at this point in time.

1 Q. WILL THE COMPANY PROVIDE AN UPDATED FAS 112 DISCOUNT RATE TO  
2 INCORPORATE THE MOST RECENT MEASUREMENT DATE?

3 A. Yes. As we have done in prior rate cases, the Company will provide updated  
4 FAS 112 costs in Rebuttal Testimony to incorporate the most recent  
5 measurement date of December 31, 2019, which will be available in late  
6 January or early February of 2020.

7

8 Q. HAS THE COMPANY INVESTIGATED WHETHER IT SHOULD USE ONLY FULLY  
9 INSURED PLANS?

10 A. Yes. The Company has evaluated fully-insuring the plans that are currently  
11 self-insured, but we determined that it was more costly to fully-insure them  
12 due to the small number of individuals covered and the degree of uncertainty  
13 around anticipated claims.

14

15 Q. HAS THE COMPANY PROVIDED THE ACTUARIAL STUDY AND DERIVATION OF  
16 THE JURISDICTIONAL AMOUNT?

17 A. Yes. Exhibit\_\_\_(RRS-1), Schedule 9, which is an actuarial study that supports  
18 the FAS 112 LTD costs for 2020-2022. Exhibit\_\_\_(RRS-1), Schedule 10  
19 shows the conversion of the 2020 total cost amounts to the NSPM electric  
20 O&M, state of Minnesota amount.

21

22 **C. Retiree Medical and FAS 112 Long-Term Disability Benefits**  
23 **Summary**

24 Q. PLEASE SUMMARIZE THE COMPANY'S REQUEST REGARDING THE MULTI-YEAR  
25 RATE PLAN AMOUNTS FOR THESE TWO BENEFITS.

26 A. The Company requests that the Commission approve retiree medical expense  
27 in the amounts of \$1.3 million, \$1.1 million, and \$1.0 million. The Company  
28 requests that the Commission approve FAS 112 long-term disability benefit

1 expense in the amounts of \$0.1 million, \$0.1 million, and \$0.1 million for  
2 2020, 2021, and 2022 respectively.

3  
4 Q. IS IT REASONABLE TO ASK CUSTOMERS TO PAY FOR RETIREE MEDICAL AND  
5 FAS 112 LONG-TERM DISABILITY BENEFIT COSTS?

6 A. Yes. It is appropriate that customers pay for these benefits because they  
7 reflect a reasonable and necessary level of expense, and because these are  
8 commitments that the Company made to employees who provided quality  
9 service to NSPM customers for many years. Stated differently, the FAS 106  
10 and 112 expenses represent benefits that our former employees have already  
11 earned, and the Company is required to comply with its obligations to disabled  
12 and retired employees. These expenses are akin to accounts payable, which  
13 are amounts the Company must pay to satisfy its legal obligations.

14  
15 **VII. BENEFIT RATE BASE ASSETS AND LIABILITIES**

16  
17 Q. WHAT TOPIC DO YOU DISCUSS IN THIS SECTION OF YOUR TESTIMONY?

18 A. I discuss the ratemaking treatment of the Company's prepaid pension asset  
19 and its unfunded liabilities.

20  
21 **A. Overview of the Prepaid Pension Asset**

22 Q. PLEASE DESCRIBE THE COMPANY'S PREPAID PENSION ASSET AND ITS  
23 UNFUNDED RETIREE MEDICAL AND POST-EMPLOYMENT BENEFIT LIABILITY.

24 A. The prepaid pension asset arises in connection with the Company's qualified  
25 pension plan. Over the life of that plan, the Company has contributed more  
26 dollars to the plan than it has recognized in actuarially calculated pension

1 expense. This results in a prepaid pension asset. Conversely, the retiree  
2 medical and post-employment benefits results in an unfunded liability.

3  
4 Q. WHAT DO YOU MEAN WHEN YOU REFER TO THE ACTUARIALLY CALCULATED  
5 EXPENSE THAT IS COMPARED TO THE CUMULATIVE CONTRIBUTIONS BY THE  
6 COMPANY?

7 A. As I discussed earlier in my testimony, the annual qualified pension expense is  
8 calculated in accordance with FAS 87 and the ACM. Similarly, the retiree  
9 medical costs are calculated under FAS 106, and post-employment benefits are  
10 calculated under FAS 112. Based on its accounting records, the Company can  
11 quantify the total amount of actuarially calculated expense for each of those  
12 benefits over the entire period that the Company has offered that benefit. If  
13 that cumulative expense amount is less than the cumulative contributions  
14 made by the Company since it began offering that benefit, the Company has a  
15 prepaid pension asset. If the cumulative recognized expense exceeds the  
16 cumulative contributions to the plan, there is an unfunded liability.

17  
18 Q. CAN YOU PROVIDE A CONCRETE EXAMPLE OF HOW A PREPAID PENSION ASSET  
19 ARISES?

20 A. Yes. Suppose that the Company contributes \$100 per year to the qualified  
21 pension trust for each of the first five years of its existence. Further suppose  
22 that the actuarially determined qualified pension expense in each of those five  
23 years is \$90. Table 11 below shows how the excess contributions each year  
24 create a cumulative prepaid pension asset

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18

**Table 11**

**Prepaid Pension Asset Example**

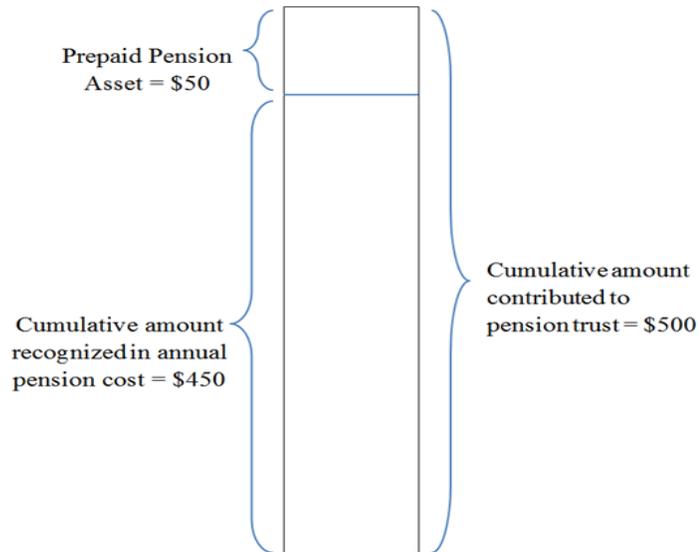
<b>Year</b>	<b>Pension Contribution</b>	<b>Pension Expense</b>	<b>Cumulative Prepaid Pension Asset</b>
1	\$100	\$90	\$10
2	\$100	\$90	\$20
3	\$100	\$90	\$30
4	\$100	\$90	\$40
5	\$100	\$90	\$50

At the end of the five-year period, the utility has a prepaid pension asset of \$50. Of course, the opposite can also occur. If pension expense exceeds the pension contributions in a given year, the prepaid pension asset will decline, or if there is no prepaid pension asset, the utility may have a pension liability. Over the long run, pension contributions and pension expense will even out, but over the short and intermediate run there will almost certainly be differences, which are recorded as prepaid pension assets or pension liabilities. Figure 1<sup>4</sup> below visually depicts the prepaid pension asset as the excess contributions over the recognized pension expense.

---

<sup>4</sup> The amounts in this figure are merely illustrative, as are the amounts in Table 11.

1 **Figure 1**



12

13

14 Q. WHY ARE THE CONTRIBUTIONS AND EXPENSE DIFFERENT IN ANY GIVEN

15 YEAR?

16 A. As I discussed earlier, the qualified pension expense calculation is governed by

17 the ACM and FAS 87, which sets forth the rules that companies must follow

18 in determining their pension costs in order to have their accounting be

19 acceptable under GAAP. In contrast, the contributions are driven by federal

20 law requirements under ERISA and the IRC. Although the expense and

21 contribution calculations both use accrual methodologies, the assumptions,

22 attribution methods, and periods of time over which the costs are required to

23 be recognized are different and thus can often result in different annual

24 amounts.

1 Q. CAN THE UTILITY WITHDRAW THE PREPAID PENSION ASSET AND USE IT TO  
2 FUND CAPITAL REQUIREMENTS OR TO PAY FOR OPERATION AND  
3 MAINTENANCE EXPENSE?

4 A. No. As I noted earlier in my discussion of the calculation of qualified pension  
5 expense, federal law prohibits the withdrawal of any amounts from the  
6 pension trust fund except for the payment of benefits and plan expenses.  
7 Once the contributions are made, they are essentially locked away.

8

9 **B. Ratemaking Treatment of Prepaid Pension Asset**

10 Q. HOW ARE PREPAID PENSION ASSETS AND UNFUNDED ACCRUED BENEFIT  
11 LIABILITIES GENERALLY TREATED FOR PURPOSES OF SETTING RATES?

12 A. Like other prepayments, a prepaid pension asset is generally treated as an  
13 addition to rate base. Conversely, FAS 106 and FAS 112 liabilities cause the  
14 rate base to decrease, which is consistent with the treatment of other  
15 unfunded liabilities.

16 Q. IS THE COMPANY PROPOSING TO APPLY THE STANDARD RATEMAKING  
17 TREATMENT OF PREPAYMENTS AND UNFUNDED LIABILITIES IN THIS CASE?

18 A. Yes. In this case, the Company is proposing to include both the prepaid  
19 pension asset and the unfunded liabilities in rate base. Because the prepaid  
20 pension asset is larger than the unfunded liability, the Company has a net asset  
21 and therefore has an increase to rate base. The Company proposes to earn a  
22 return on the asset at the Company's weighted average cost of capital  
23 (WACC).

1 Q. IS THE COMPANY PROPOSING TO EARN A RETURN ON THE FULL AMOUNT OF  
2 THE NET PREPAID PENSION ASSET?

3 A. No. The net amount of the asset will be further offset by the accumulated  
4 deferred income tax amounts (ADIT) associated with it. Thus, instead of  
5 earning a return on the full amount of the net asset (i.e., the prepaid pension  
6 asset less the unfunded accrued liabilities of retiree medical and post-  
7 employment benefits) the Company earns a return only on the portion that  
8 remains after the ADIT is adjusted from it.

9

10 Q. HOW DOES ADIT ARISE IN CONNECTION WITH THE PREPAID PENSION ASSET  
11 OR ACCRUED UNFUNDED LIABILITY?

12 A. When the Company makes a contribution, it is allowed to deduct the  
13 contribution amount (up to IRS-imposed limits). That deduction shields  
14 income from taxes, which gives rise to deferred taxes. Thus, the amount by  
15 which the contributions in a particular year exceed the annual recognized cost  
16 for that year gives rise to a deferred tax liability. The opposite situation occurs  
17 when the annual cost recognized for a particular benefit exceeds the  
18 contribution, which give rise to a deferred tax asset. Company witness Mr.  
19 Halama discusses ADIT and how it impacts our filing.

20

21 Q. WHAT AMOUNT OF BENEFIT ASSETS AND LIABILITIES IS INCLUDED IN THE TEST  
22 YEAR RATE BASE?

23 A. Table 12 below shows the amount included in rate base for all benefit types  
24 included in 2016. This table also shows the amounts that must be offset by  
25 the ADIT associated with the benefit asset or liability balance. This same  
26 information can also be found in the Non-Plant Rate Base (Assets/Liabilities)  
27 Schedule. The net balance is approximately \$82.4 million on a Minnesota

1 electric jurisdictional basis. This amount should be added to the Company's  
 2 rate base because it represents shareholder capital held for future use and that  
 3 will reduce ratepayer costs in those years, providing ratepayer benefit.

4  
 5 **Table 12**  
 6 **Pension and Benefits Assets and Liabilities (\$)**

7 <b>Rate Base Benefit (Short and Long-Term)</b>	8 <b>Non-Plant Rate Base Asset/(Liability)</b>	9 <b>Associated Accumulated Deferred Tax Asset/(Liability)</b>	10 <b>Net Rate Base Impact Asset/(Liability)</b>
11 Prepaid Pension Asset	160,632,037	(45,192,860)	115,439,178
12 Retiree Medical - FAS 106	(34,795,006)	9,789,366	(25,005,640)
13 Post-Employment Benefits FAS 112	(10,397,766)	2,925,349	(7,472,417)
14 Total	115,439,266	(32,478,145)	82,440,261

15 Q. WHAT IS THE COMPANY'S REQUEST WITH RESPECT TO THE NET PENSION ASSET  
 16 BALANCE OF \$82.4 MILLION?

17 A. The Company seeks Commission approval to add that amount to its rate base  
 18 and earn its WACC on that balance, consistent with the treatment of other  
 19 prepayments.

20 Q. HAS THE COMPANY CREATED A SCHEDULE TO REFLECT THE UNDERLYING  
 21 CALCULATION OF THE PREPAID PENSION ASSET THAT IS INCLUDED IN THE  
 22 MULTI-YEAR RATE PLAN PERIOD, 2020-2023?

23 A. Yes. Exhibit\_\_\_\_(RRS-1), Schedule 13 shows the annual calculation of the  
 24 total NSPM prepaid pension asset or liability from 2015 through 2022.  
 25 Schedule 13 also shows a detailed calculation by month that supports the  
 26 2020-2023 NSPM electric state of Minnesota prepaid pension asset balances  
 that are being requested in rate base for this case.

1 Q. WHAT HAS CAUSED THE RECENT GROWTH OF THE PREPAID PENSION ASSET?

2 A. The growth of the prepaid pension asset was driven by three factors, all of  
3 which were outside the Company's control. The first factor was the  
4 enactment by Congress of the Pension Protection Act of 2006. Prompted by  
5 the defaults by several large defined benefit pension plans in the early part of  
6 that decade, Congress passed legislation that gave defined benefit pension  
7 plans seven years to become 100 percent funded. The Pension Protection Act  
8 also created penalties for plans that are underfunded, including an increase in  
9 Pension Benefit Guaranty Corporation (PBGC) premiums. As I will explain  
10 in more detail later in my testimony, the PBGC was established by Congress  
11 to insure pension benefits under private-sector defined benefit pension plans.  
12 The PBGC is funded by premiums paid by plan sponsors and by investment  
13 returns on the assets held in the PBGC trust fund.

14

15 The second factor was the severe economic downturn that occurred in 2008.  
16 The steep drop in equities markets dramatically reduced the net asset value of  
17 pension plans across the United States, including those of Xcel Energy. The  
18 Xcel Energy pension plans, for example, lost approximately 26 percent of  
19 their value as a result of the market crash.

20

21 The third factor was the drop in interest rates, which was caused by the  
22 Federal Reserve's efforts to stimulate the national economy in the wake of the  
23 2008 recession. The resulting drop in discount rates caused the Company's  
24 pension liabilities to become larger, which increased the amount of  
25 underfunding. This is because future pension liabilities are discounted to  
26 present value, and a higher discount rate reduces the liability balance, whereas  
27 a lower discount rate increases the liability balance. That liability balance is

1 then compared to the value of the trust assets to determine its funded status  
2 and whether the trust is overfunded or underfunded.

3  
4 Q. HOW DID THE COMPANY RESPOND TO THE COMBINATION OF HEIGHTENED  
5 FUNDING REQUIREMENTS AND A LOWER FUNDING LEVEL IN ITS PLANS?

6 A. The Company responded by taking the only steps that were practically  
7 available to it, which was to provide additional funding to the pension plans.  
8 To help ensure that the pension plans complied with the Pension Protection  
9 Act by becoming fully funded within seven years, the Company made the  
10 contributions listed in Exhibit\_\_\_(RRS-1), Schedule 13. As I mentioned  
11 previously, these contributions will be recognized as expense over future  
12 periods. This timing difference gives rise to the prepaid pension asset.

13  
14 Q. HOW CAN THE PENSION PLAN BE UNDERFUNDED AND YET THE COMPANY HAS  
15 A PREPAID PENSION ASSET?

16 A. The Company can have an underfunded pension plan at the same time it has a  
17 prepaid pension asset because they measure different things. The unfunded  
18 pension plan occurs when the projected benefit obligation exceeds the fair  
19 value of the pension plan assets. A prepaid pension asset occurs when the  
20 cumulative cash contributions to the trust exceed the cumulative pension  
21 expense recognized under FAS 87 since the inception of the pension plan.

22  
23 **C. Justification for Including the Net Asset in Rate Base**

24 Q. WHY IS IT APPROPRIATE TO INCLUDE THE NET ASSET IN RATE BASE?

25 A. The net asset should be included in rate base for two separate and  
26 independent reasons. First, as I explained earlier, it is a well-established  
27 regulatory principle for prepayments to be included in rate base, regardless of

1 whether they are prepayments by the utility or by its customers. In other  
2 words, prepayments are included regardless of whether they are additions or  
3 reductions to rate base. There is no reason to treat the net prepayment in this  
4 case differently.

5  
6 Second, customers are receiving the benefit of a return on the prepaid pension  
7 asset, and therefore it is appropriate that the Company earn a return on its  
8 prepayment as well.

9  
10 Q. PLEASE EXPLAIN WHAT YOU MEAN WHEN YOU STATE THAT CUSTOMERS ARE  
11 RECEIVING THE BENEFIT OF A RETURN ON THE PREPAID PENSION ASSET.

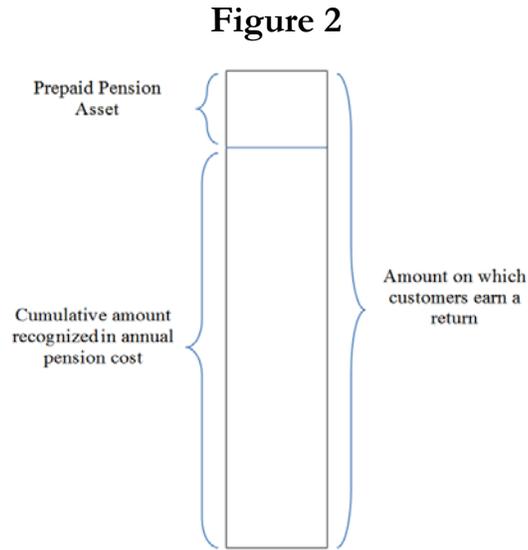
12 A. As I explained earlier in my testimony, the annual pension cost determined  
13 under both accounting methods, the ACM (NSPM Plan) and FAS 87 (XES  
14 Plan), includes an EROA. The EROA percentage is multiplied by the value of  
15 the assets in the pension trust, and the product of that calculation is subtracted  
16 from the annual pension cost. Thus, the return on the prepaid pension asset  
17 reduces the annual pension cost passed on to ratepayers.

18  
19 Q. WHAT IS THE EROA FOR THE NSPM PLAN AND THE XES PLAN?

20 A. The EROA for both the NSPM Plan and the XES Plan is 7.10 percent for  
21 2020, 2021, and 2022. That percentage is applied to the balance in the  
22 pension trust.

23  
24 Q. DOES THE PENSION TRUST FUND BALANCE THAT IS MULTIPLIED BY THE  
25 EROA INCLUDE THE PREPAID PENSION ASSET?

1 A. Yes. As shown in Figure 2 below, customers receive the benefit of the  
2 earnings on the *entire* amount of assets in the pension trust, not just the  
3 amount that has been recognized in annual pension cost.



14

15 As the figure shows, customers are receiving a return on amounts that they  
16 have not yet paid through recognized pension cost. In effect, the Company  
17 has made a prepayment of pension contributions, and customers are earning a  
18 return on that prepayment at the EROA. The return is reflected as a decrease  
19 in annual pension cost. It would be inequitable and unreasonable to deny the  
20 Company a return on the prepaid pension asset at the WACC because  
21 customers are, in fact, receiving the benefit of a return on that prepayment at  
22 the EROA.

23

24 Q. YOU TESTIFIED EARLIER THAT THE EROA FOR THE COMPANY IS 7.10  
25 PERCENT, WHEREAS THE COMPANY IS SEEKING A WACC OF 7.42 PERCENT IN  
26 THE TEST YEAR. DOES THE DISPARITY BETWEEN THE WACC AND THE

1 EROA DEMONSTRATE THAT CUSTOMERS ARE DISADVANTAGED BY THE USE  
2 OF THE WACC AS THE RETURN ON THE PREPAID PENSION ASSET?

3 A. No. The disparity between the WACC and the EROA is offset by the  
4 benefits that customers receive through avoidance of incremental PBGC  
5 premiums.

6  
7 The PBGC is a federal agency established by Congress as part of ERISA to  
8 insure pension benefits under private sector defined benefit pension plans. If  
9 a pension plan is terminated without sufficient money to pay all benefits,  
10 PBGC's insurance program will pay employees the benefits promised under  
11 the pension plan, up to the limits set by law. The funding for the PBGC  
12 comes partly from premiums charged to pension sponsors and partly from  
13 returns on assets held by the PBGC.

14  
15 Q. WHAT TYPES OF PREMIUMS DOES THE PBGC CHARGE?

16 A. The PBGC charges two types of premiums: (1) a per capita premium that is  
17 charged to all single-employer defined benefit plans; and (2) a variable  
18 premium charged to underfunded plans. The amounts of the premiums are  
19 set by Congress and must be paid by sponsors of the defined benefit plans,  
20 such as NSPM.

21  
22 Q. ARE THE VARIABLE PREMIUMS APPLICABLE TO UNDERFUNDED PLANS  
23 INCREASING?

24 A. Yes. For 2018, the variable-rate premium for a single-employer plan such as  
25 that of NSPM is \$38 per \$1000 of unfunded vested benefits.

1 Q. ARE THE COMPANY'S PENSION PLANS CURRENTLY UNDERFUNDED?

2 A. Yes. And absent the prepaid pension asset, the plan would be further  
3 underfunded.<sup>5</sup>

4

5 Q. BY HOW MUCH WOULD THE PENSION PLANS BE UNDERFUNDED IN THE  
6 ABSENCE OF THE PREPAID PENSION ASSET?

7 A. In the absence of the prepaid pension asset, the NSPM Plan would be further  
8 underfunded by \$184 million at the end of 2018.

9

10 Q. BY HOW MUCH WOULD THE PBGC PREMIUMS INCREASE IN 2018 IN THE  
11 ABSENCE OF THE PREPAID PENSION ASSET?

12 A. The PBGC premiums would be approximately \$3.0 million higher in 2018 on  
13 a NSPM Electric, state of Minnesota basis, without the prepaid pension asset.

14

15 Q. ARE PBGC PREMIUMS INCLUDED IN THE ANNUAL PENSION COST?

16 A. Yes. PBGC premiums are included in the annual pension cost calculation.  
17 Therefore, the existence of the prepaid asset will avoid the need for NSPM's  
18 electric retail customers to pay an additional \$3.0 million in 2018.

19

20 Q. DOES THE AVOIDANCE OF INCREMENTAL PBGC PREMIUMS OFFSET THE  
21 PERCENTAGE DIFFERENCE BETWEEN THE EROA AND THE WACC?

22 A. Yes. As I testified earlier, the EROA is 7.10 percent, whereas the WACC  
23 requested by the Company in this case is 7.42 percent, which is a difference of  
24 32 basis points. Multiplying the \$82 million net asset by 32 basis points yields

---

<sup>5</sup> A plan can be underfunded at the same time it has a prepaid pension asset because they measure different things. As I testified earlier, the prepaid pension asset is the amount by which cumulative contributions exceed cumulative recognized pension expense. A pension plan is underfunded when its pension benefit obligations exceed the value of its assets.

1 a total of approximately \$264,000, which is the amount by which the return to  
2 the Company will exceed the expected return to customers. That amount is  
3 far smaller than the \$3.0 million that customers avoid paying in PBGC  
4 premiums because of the existence of the prepaid asset. Thus, it is reasonable  
5 to include the net asset in rate base and for the Company to earn a WACC  
6 return on the asset.

7  
8 Q. PLEASE SUMMARIZE THE COMPANY'S REQUEST WITH RESPECT TO THE PREPAID  
9 PENSION ASSET.

10 A. The Company requests that the prepaid pension asset be included in rate base  
11 and that it earn a return at the WACC, similar to other prepayments.

## 12 13 **VIII. ACTIVE HEALTH AND WELFARE COSTS**

14  
15 Q. WHAT ARE THE ACTIVE HEALTH AND WELFARE AMOUNTS FOR 2020, 2021, AND  
16 2022?

17 A. The 2020, 2021, and 2022 health and welfare expense amounts are  
18 approximately \$38.4 million, \$39.9 million, and \$41.5 million, respectively.

19  
20 Q. WHAT TYPES OF BENEFIT COSTS ARE INCLUDED IN ACTIVE HEALTH AND  
21 WELFARE?

22 A. Active health and welfare costs can be broken down into three categories.  
23 The first and largest category is for active healthcare costs; the second  
24 category is for miscellaneous benefit programs and costs; and the third  
25 category contains life, LTD, and business travel insurance premiums.

1 Q. SINCE ACTIVE HEALTH AND WELFARE CONSISTS OF THREE CATEGORIES OF  
2 COSTS, CAN YOU PROVIDE A FURTHER BREAKDOWN OF COSTS IN THE TEST  
3 YEAR?

4 A. Yes. Exhibit\_\_\_(RRS-1), Schedule 14, shows the components that are  
5 included in each category and the amount for each component in the test year.  
6 The active healthcare category makes up 90 percent of the total health and  
7 welfare costs, so the remainder of this section of testimony will focus on  
8 active healthcare.

9

10 Q. WHAT TYPES OF COSTS ARE INCLUDED IN ACTIVE HEALTHCARE?

11 A. Active healthcare costs are all costs associated with providing healthcare  
12 coverage to our employees. As explained in more detail by Ms. Lowenthal,  
13 active healthcare benefits include medical, pharmacy, dental and vision claims,  
14 administrative fees, employee withholdings, pharmacy rebates, Health Savings  
15 Account (HSA) contributions, transitional reinsurance fees, trustee fees,  
16 interest income and opt-out finding.

17

18 Q. DID THE COMPANY MAKE ANY ADJUSTMENTS TO THE PER BOOK AMOUNTS  
19 FOR ACTIVE HEALTHCARE CLAIMS?

20 A. Yes. Table 13 below shows both the per book and actual incurred amounts of  
21 active health and welfare claims for the five years prior to the test year and for  
22 the 2020-2022.

**Table 13**  
**Active Health Care**  
**Per Book and Actual Incurred Claims**

<b>NSPM Electric O&amp;M State of MN (\$)</b>			
<b>Year</b>	<b>Per Book Amount</b>	<b>Actual Incurred Claims</b>	
		<b>IBNR Adjustment</b>	<b>Actual Incurred Claims</b>
2015	37,332,663	570,047	37,839,710
2016	38,267,972	(105,005)	38,162,967
2017	33,501,711	740,938	34,242,649
2018	34,120,041	(263,278)	33,856,764
2019 Forecast	33,211,673	319,203	33,530,876
2020 Test Year	n/a	n/a	34,547,977
2021 Plan Year	n/a	n/a	35,966,484
2022 Plan Year	n/a	n/a	37,505,915

16 Q. WHY WAS IT NECESSARY TO MAKE AN ADJUSTMENT TO THE PER BOOK CLAIMS  
17 AMOUNT?

18 A. This adjustment is necessary to reflect actual costs incurred in each year. The  
19 per book amounts for active healthcare include estimates because there is  
20 generally an average lag of approximately 30 days between when healthcare is  
21 provided and when the Company receives a bill for that care. Therefore, the  
22 actual amount of active healthcare expense was not available at the time the  
23 Company recorded its per book amount at the end of each month. Because  
24 the Company needs to close its books at the end of each reporting period  
25 before it receives all of those healthcare claims, it takes the actual amounts  
26 recorded through a certain point in the year and estimates the additional  
27 amount that will be incurred but not reported (IBNR) by the end of the

1 reporting period. This accrual estimate is called the IBNR reserve. During the  
2 following period, the Company receives the actual amounts attributable to care  
3 provided in the last part of the prior period, and at that time it trues up the  
4 IBNR estimate to the actual incurred amount. Therefore, the per book  
5 amounts need to be adjusted so that they reflect the actual incurred claim  
6 amounts during that period. After the adjustment, the periods include only  
7 the actual amounts incurred for the twelve months.

8  
9 Q. HOW WERE THE 2020-2022 ACTIVE HEALTHCARE COSTS DETERMINED?

10 A. With the exception of medical and pharmacy claims, the Company's actuary,  
11 Willis Towers Watson, calculated the test year amounts by using actual  
12 experience, adjusting it for any plan design changes, participant counts,  
13 regulations, administrative fees, etc., and then trended that amount forward.

14  
15 Q. HOW WERE THE 2020-2022 MEDICAL AND PHARMACY COSTS DETERMINED?

16 A. Since medical and pharmacy claims make up over 95 percent of the total  
17 health and welfare amounts, the Company wanted to ensure that it calculated  
18 these two components using the most current information available. The  
19 Company first took the most recent 2019 forecasted incurred medical and  
20 pharmacy claims amount, after making the IBNR adjustments described  
21 above, and then applied a 5.50 percent healthcare trend increase over the three  
22 years of the multi-year plan.

23  
24 Q. WHAT IS THE COMPANY'S BASIS FOR USING A 5.50 PERCENT MEDICAL AND  
25 PHARMACY HEALTHCARE TREND?

26 A. The assumption reflects Willis Towers Watson's overall expectation of  
27 healthcare cost increases based on survey averages, carrier information, and an

1 analysis of the broad healthcare market. Exhibit\_\_\_(RRS-1), Schedule 15  
 2 provides a summary of this analysis. Overall, the Willis Towers Watson  
 3 survey data indicates that medical costs are expected to rise between 5.5  
 4 percent and 7.50 percent in 2019. While, PricewaterhouseCoopers (PwC)  
 5 estimates that medical and pharmacy costs will rise 6.00 percent in 2019. This  
 6 information, which was gathered by PwC’s Health Research Institute, was  
 7 based on PwC’s own internal research and input from health plan actuaries,  
 8 industry leaders, analyst reports, and employer surveys. Finally, the Aon  
 9 Carrier Trend Report expects 2019 medical costs to increase by 7.00 percent  
 10 and 2019 pharmacy costs to increase by 7.50 percent.

11  
 12 Q. WHAT PERCENTAGE DOES TOTAL HEALTH AND WELFARE COSTS INCREASE  
 13 FROM 2020-2023 AFTER USING THE METHODOLOGY DESCRIBED ABOVE?

14 A. As shown in Table 14 below, the amounts reflect an average increase of 3.8  
 15 percent, which is well below the overall 5.50 percent healthcare trend increase.

16 **Table 14**  
 17 **Active Health Care Expense**

NSPM Electric O&M State of MN				
	2019 Forecast	2020 Test Year	2021 Plan Year	2022 Plan Year
Active Healthcare (\$)	33,530,876	34,547,977	35,966,484	37,505,915
Year-Over-Year Change		3.06%	4.11%	4.28%

18  
 19  
 20  
 21  
 22  
 23 Q. DO YOU BELIEVE THE COMPANY’S ESTIMATE OF HEALTHCARE COSTS IS  
 24 REPRESENTATIVE OF COSTS THE COMPANY EXPECTS TO INCUR IN FUTURE  
 25 YEARS?

26 A. Yes. As shown in Table 14 above, the Company’s active healthcare costs are  
 27 currently forecasted to grow approximately 3-4 percent per year for 2020,

1 2021, and 2022. This growth rate is lower than the typical rate for other  
2 organizations, as demonstrated by the attachment referred to above. The  
3 Company has implemented several plan design changes to help control the  
4 pace of growth, as discussed by Company witness, Ms. Lowenthal. However,  
5 active healthcare costs have continued to increase and the Company's  
6 forecasts through 2022 are reasonable.

7  
8 Q. WHY IS IT REASONABLE FOR CUSTOMERS TO PAY ACTIVE HEALTH AND  
9 WELFARE COSTS INCURRED BY THE COMPANY?

10 A. It is appropriate that customers pay for these benefits because they reflect a  
11 reasonable and necessary level of expense. Employees expect their employer  
12 to provide a reasonable level of health and welfare benefits, and any employer  
13 that does not do so is at a significant disadvantage in the labor market. Thus,  
14 our compensation plans and benefits are required to attract, retain, and  
15 motivate employees needed to perform the work necessary to provide quality  
16 services for NSPM customers.

17  
18 **IX. WORKERS' COMPENSATION FERC 925 COSTS**

19  
20 Q. WHAT TYPES OF COSTS ARE INCLUDED IN FERC ACCOUNT 925 INJURIES AND  
21 DAMAGES?

22 A. FERC Account 925 is composed of workers' compensation coverage and  
23 other liability insurance costs. The workers' compensation benefit covers  
24 work-related injury costs for medical claims, permanent or partial disability,  
25 lost time, rehabilitation costs, prescription drugs, etc. The other liability  
26 insurance includes coverage for general liability, excess liability, fiduciary  
27 insurance, and directors' and officers' insurance. Because my area of

1 responsibility is in benefits accounting, my testimony is limited to the workers'  
2 compensation costs.

3  
4 Q. PLEASE EXPLAIN HOW WORKERS' COMPENSATION COSTS ARE DETERMINED.

5 A. Similar to LTD costs, the accounting treatment for workers' compensation  
6 differs for the self-insured and fully-insured portions of the plan. The  
7 workers' compensation benefit is self-insured for any active bargaining or  
8 non-bargaining employee who was injured before August 1, 2001, and it is  
9 fully insured for any employee who was injured on or after that date. The  
10 Company is required to accrue for self-insured workers' compensation costs  
11 under FAS 112. The fully-insured portion is the cost of the insurance  
12 premiums that the Company must pay each year.

13  
14 Q. WHAT HAS BEEN THE TREND FOR THE WORKERS' COMPENSATION COSTS OVER  
15 THE LAST SEVERAL YEARS AND FOR THE MULTI-YEAR RATE PLAN PERIOD?

16 A. Table 15 below compares the workers' compensation benefit costs from 2015  
17 through 2022.

18 **Table 15**  
19 **Workers' Compensation Expense**

20 **NSPM Electric O&M State of MN (\$)**

21 <b>Year</b>	<b>FAS 112</b>	<b>Insurance Premiums &amp; Other</b>	<b>Total Workers' Compensation</b>
22 2015	471,615	2,515,087	2,986,703
23 2016	454,589	1,856,452	2,311,041
24 2017	255,880	1,914,890	2,170,770
25 2018	157,468	1,880,119	2,037,587
2019 Forecast	(710,247)	1,907,971	1,197,725
2020 Test Year	123,281	1,888,992	2,012,273
2021 Plan Year	114,959	1,880,990	1,995,949
2022 Plan Year	106,239	1,873,035	1,979,274

1 Q. HOW DID YOU CALCULATE THE WORKERS' COMPENSATION AMOUNTS FOR  
2 2020 THROUGH 2022?

3 A. The FAS 112 amounts are based on the 2020 through 2022 projected cost  
4 amounts from the Willis Towers Watson actuarial calculation provided in May  
5 2019. The insurance premium amounts were based on the actual premiums  
6 paid through October 2019, with annual increases of five percent applied to  
7 trend to the end of 2022.

8

9 Q. HAS THE COMPANY PROVIDED THE ACTUARIAL STUDY AND DERIVATION OF  
10 THE JURISDICTIONAL AMOUNT?

11 A. Yes. The Company has included Exhibit\_\_\_(RRS-1), Schedule 9, which is an  
12 actuarial study that supports the FAS 112 workers compensation costs in  
13 2020-2022. Exhibit\_\_\_(RRS-1), Schedule 10 shows the conversion of the  
14 2020 total cost amounts to the NSPM electric O&M, state of Minnesota  
15 amount.

16

17 Q. IS THE COMPANY SEEKING TO RECOVER THE FORECASTED WORKERS'  
18 COMPENSATION EXPENSE AS SHOWN IN TABLE 15 AS PART OF ITS MULTI-YEAR  
19 RATE PLAN?

20 A. Yes. Mr. Halama has incorporated the budgeted amounts into the 2020 test  
21 year and 2021 and 2022 plan year revenue requirements. These costs are  
22 calculated in accordance with accounting rules and standards and are based on  
23 actuarial assumptions specific to the Company.

1 **X. CONCLUSION**

2

3 Q. PLEASE SUMMARIZE YOUR TESTIMONY AND RECOMMENDATIONS.

4 A. The assumptions that the Company has used to determine the test year  
5 pension expense are reasonable, as shown by comparison with other utilities’  
6 pension assumptions. In addition, we are proposing to use a five-year average  
7 discount rate – as the Commission approved in our last rate case – to reduce  
8 the potential number of disputed issues in this current case. Our annual  
9 qualified pension expense decreases each year through the multi-year rate plan  
10 period, in part due to the benefit plan design changes that have reduced  
11 employee benefit levels.

12

13 The Company should be allowed to recover the costs of its FAS 106 post-  
14 retirement medical benefit and its FAS 112 benefit. Those are reasonable  
15 costs that are part of the total compensation package the Company needs to  
16 attract and retain good employees.

17

18 The Company should also be allowed to include its prepaid pension asset in  
19 rate base. The gains from that asset help reduce pension expense in the test  
20 year, but shareholders have no access to those gains. The Company requests  
21 that the prepaid pension asset be included in rate base and that it earn a  
22 return, similar to other prepayments.

23

24 Regarding healthcare costs, we have implemented measures to help control  
25 the pace of growth in our healthcare costs, and the result is reflected in a  
26 lower inflation factor during the multi-year rate plan period than that  
27 recommended by our actuaries and PwC.

1 Finally, our workers' compensation costs are necessary and the forecasted  
2 amounts presented in my testimony should be approved for recovery in rates.

3  
4 In summary, and as discussed in more detail by Ms. Lowenthal, the non-cash  
5 employee benefits discussed in my testimony are part of the Company's  
6 overall compensation and benefits package and are necessary to attract and  
7 retain the employees required to provide high-quality service to our customers.  
8 The forecasted amounts of pension and benefits costs I present are reasonable  
9 and accurately reflect our expected pensions and benefits expense in the multi-  
10 year rate plan period. As such, I recommend that the Commission approve  
11 these levels of expense to be included in rates.

12  
13 Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

14 A. Yes, it does.