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IN THE MATTER OF THE APPLICATION OF
NORTHERN STATES POWER COMPANY,
D/B/A XCEL ENERGY, FOR AUTHORITY TO
INCREASE RATES FOR ELECTRIC SERVICE
IN MINNESOTA

MPUC Docket No. E-002/GR-13-868
OAH Docket No. 68-2500-31182

**EXCEPTIONS
OF THE MINNESOTA DEPARTMENT OF COMMERCE**

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INTRODUCTION

The Minnesota Department of Commerce, Division of Energy Resources, Energy Regulation and Planning Unit (the Department or DOC) appreciates the thorough and detailed work of the Administrative Law Judge (ALJ) regarding this complex, voluminous matter, and respectfully submits to the Minnesota Public Utilities Commission (Commission) the following limited Exceptions to the Recommendation and Report (Report) of the ALJ:

1. Rate of Return – Return on Equity (Issue 1);¹
2. Passage of Time – Depreciation and Plant Retirements in the 2015 Step (Issue 10);
3. Changes in In-Service Dates of Capital Projects in 2014 and the 2015 Step (Issue 11); and
4. Qualified Pension – Discount Rate (Issue 4) and 2008 Market Loss (Issue 5).

Moreover, the Department affirmatively supports the ALJ's recommendation as to Rate Case and Monticello Prudency Review Expense Amortization (Issue 8) on pages 107-109 of the Report. Finally, while it continues to support its positions on contested issues that the ALJ did not support, the Department offers no additional argument through filed exceptions regarding those issues.

¹ Issue numbers refer to the number designated in the Final Issues List filed by the Company on October 7, 2014.

EXCEPTIONS

I. RATE OF RETURN – RETURN ON EQUITY

A. RATE OF RETURN: DR. AMIT’S TESTIMONY SUPPORTS A RETURN ON EQUITY OF 9.64 PERCENT (WITH FLOTATION COSTS) FOR XCEL, RATHER THAN 9.77 PERCENT IN THE ALJ REPORT

The Department continues to support Dr. Amit’s recommended Return on Equity (ROE) for Xcel of 9.64 percent with flotation costs and, thus, respectfully takes exception to the ALJ Report’s recommended return on equity (ROE) of 9.77 percent.² In particular, the record does not support the Report’s recommendation that a higher ROE than the results of Dr. Amit’s Discounted Cash Flow (DCF) analysis is warranted. Determination of a reasonable ROE is a quasi-judicial function of the Commission and its decision must be based upon the facts in the record.³

1. Fundamentals of ROE Analysis

Determining a reasonable ROE for Xcel must be based on reasoned analysis; it would not be appropriate, for example, to search for a desired outcome regardless of the flaws in a model that might produce such an outcome. Nor is a comparison of the parties’ ROE numbers sufficient foundation to determine the reasonableness of a particular ROE figure. Rather, as the Department demonstrated in great detail through the testimony of Dr. Amit, the key to a reasonable ROE for Xcel is reliance on a properly applied DCF method, based on reasonable inputs, together with confirmation of the reasonableness of the DCF analysis by use of a properly applied Capital Asset Pricing Model (CAPM) analysis.⁴ Having checked the reasonableness of

² ALJ Report Proposed Finding 373.

³ *In re Application of Minn. Power for Authority to Increase Rates for Electric Serv. in Minn.*, 838 N.W.2d 747, 760 (Minn. 2013).

⁴ Ex. 400 at 41-44, (Amit Direct); DOC Ex. 403 at 5-8 (Amit Surrebuttal).

his DCF analyses through his application of CAPM, the results of Dr. Amit's DCF analysis of 9.64 percent (with flotation costs) is well-supported in the record as a reasonable ROE for Xcel.⁵

Thus, on this issue, the Department takes exception to Findings 373, 380,382, 383 and 385.

2. Exception to Proposed Finding 373

ALJ Report Proposed Finding 373 states:

373. After carefully considering the evidence in the record, the Administrative Law Judge recommends that the Commission approve a Return on Equity of 9.77 percent.

The Department disagrees with this recommendation because the reasons provided by the ALJ for recommending a Return on Equity of 9.77 percent are not supported by the record and are counter to fundamental financial principles. Proposed Finding 373 should be amended as follows:

373. After carefully considering the evidence in the record, ~~the Administrative Law Judge recommends that the Commission~~ should approve a Return on Equity of ~~9.77~~ 9.64 percent.

Below is the Department's discussion of its disagreement with each of the reasons provided by the ALJ.

3. Exception to Proposed Finding 380

The ALJ Report Proposed Finding 380 states:

380. Normally, more recent information will better reflect expectations regarding the expected ROE for the Company. Use of a single, shorter time period for averaging, however, can lead to anomalous results. The averaging period should be reasonably representative of expected capital market conditions over the long term.

⁵ Ex. 403 at 4-8 (Amit Surrebuttal).

The Department notes that Proposed Finding 380 is not supported by prefiled testimony of any witness, including Company witness Mr. Hevert. The statement that single shorter time periods for averaging, can lead to anomalous results, first and only appeared in Mr. Hevert's Opening Statement, *with no analytical support*. Moreover, there is nothing in the record to demonstrate that Dr. Amit's 30-day average used in his surrebuttal testimony is somehow anomalous.

Additionally, there is nothing in the record that explains the concept of "anomalous results" as related to the calculation of average dividend yields.

Finally, the statement that "the averaging period should be reasonably representative of expected capital market conditions over the long term" does not provide any support for the notion that a longer time period for averaging dividend yields better reflects the expected capital market conditions over the long term.

To the contrary, as Dr. Amit explained, the current price per share incorporates all relevant publicly available information, so non-recent historical prices should be avoided in calculating the dividend yield.⁶⁶ The notion that using a longer time period to calculate dividend yields better reflects the expected capital market conditions over the long run is conceptually wrong. Use of non-current data would unreasonably allow irrelevant information to set rates. Instead, current market data including current dividend yields best reflects the expected capital market conditions, not only in the short run, but in the long run as well. Thus, the last set of current (30-day) data used is the most appropriate market data to represent the expected capital

⁶⁶ Ex. 400 at 24 and 57-58 (Amit Direct).

market conditions over the long term. Using older historical data over a longer time period is simply irrelevant to expected capital market conditions.

Proposed Finding 380 should be amended as follows:

380. Normally, more recent information will better reflect expectations regarding the expected ROE for the Company. Use of a single, shorter time period for averaging, however, can lead to anomalous results when there are clear indications that the financial markets are abnormal. No such indications exist for this rate case. The averaging period should be reasonably representative of expected capital market conditions ~~over the long term.~~

4. Exception to Proposed Finding 382

Proposed Finding 382 states:

382. In this case, however, the Administrative Law Judge concludes that the record shows that the 30-day period used in the Department's Surrebuttal testimony may not be representative of the time period in which the ROE will remain in effect. More specifically, the record shows that the dividend yields used in the Department's Surrebuttal Testimony were significantly lower than the dividend yields used in its Direct Testimony, falling by 54 and 26 basis points, respectively, from the Department's initial analysis. These decreased dividend yields were the result of unusually high stock prices during the June-July 2014 time period used in the Department's Surrebuttal Testimony. Since that time, utility stock prices have declined relative to the overall stock market and moved more in line with historic expectations. As a result, the Department's updated 30-day dividend yields included in its Surrebuttal Testimony may reflect a short-term anomaly. [footnotes omitted]

The Department concludes that the Proposed Finding 382 is neither supported by the record, nor supported by any reasonable financial analysis.

In Proposed Finding 381, the Report explained that in Xcel's last rate case, the ALJ adopted the Department's position of the most recently available 30-day period because that time period was sufficiently long and the Department's more recent data was a better reflection of then-current market expectations than the Company's older data.

However, the basis for the decisions in the prior rate case also apply to the instant case, and there is no valid justification to substitute Proposed Finding 382 for the Proposed Finding 381, pertaining to the prior rate case. The following reasons listed in Proposed Finding 382 for rejecting the Department's Surrebuttal 30-day period do not adequately support this change:

- The 30-day period used by the Department in its Surrebuttal Testimony may not be representative of the time period in which the ROE will remain in effect.
- The dividend yields used by the Department in its Surrebuttal Testimony were significantly lower than in its initial testimony because the unusually high stock prices have declined relatively to the overall stock market. As a result, the Department's updated 30-day dividend yields may reflect a short-term anomaly.

First, neither statement is supported by any testimony provided by the Company's expert, Mr. Hevert since the first time they appeared was in Mr. Hevert's Opening Statement, without support.

Second, a basic financial principal postulates that the most currently available dividend yields (and projected growth rates) are the best predictors for the ROE for any time into the future until new, more recent market data is used.⁷ There is no reasonable link between the length of the historical period used to calculate the dividend yields and the period for which the ROE would remain in effect.

Third, the statement that, because the lower dividend yields calculated in the Department's Surrebuttal Testimony increased significantly after the period June-July, 2014, such dividend yields may reflect a short-term anomaly, is without merit.

⁷ *Id.*

In its reply brief,⁸ the Department demonstrated that utility stock prices over the period June-July, 2014 did not represent a short-term anomaly. The Department explained:

Moreover, the Company's claim that utility valuation was unusually high during the period June-July, 2014 is not supported by publicly available information. To assess this claim, it is reasonable to examine the valuation of the well-known iShares U.S. Utilities Index Fund (IDU). Over the period June 7, 2014 through July 7, 2014, the average price for IDU was \$106.70, compared to an essentially unchanged price of \$106.26 on October 3, 2014.⁹ Clearly then, there was no material change in electric utility valuation for these periods, and the period June-July, 2014 reflected investors' expectations about the future prices of electric utilities.

Moreover, Table 1 below shows the monthly average closing prices for the IDU over the period June-December, 2014.

Table 1: Monthly Changes of iShares U.S. Utilities Index Fund (IDU) Price¹⁰

Month	Average Monthly Closing Price	Month to Month Percentage Change of Closing Price
June	\$107.45	-0.98%
July	\$106.39	-1.88%
August	\$104.39	-1.88%
September	\$106.33	1.86%
October	\$108.37	2.39%
November	\$114.71	5.37%
December	\$117.16	2.13%

From Table 1, it is clear that if a short-term anomaly exists, it was the temporary *lower* utility prices in July and August, 2014. Since then, for the period September-December, 2014,

⁸ DOC Reply Br. at 7-8.

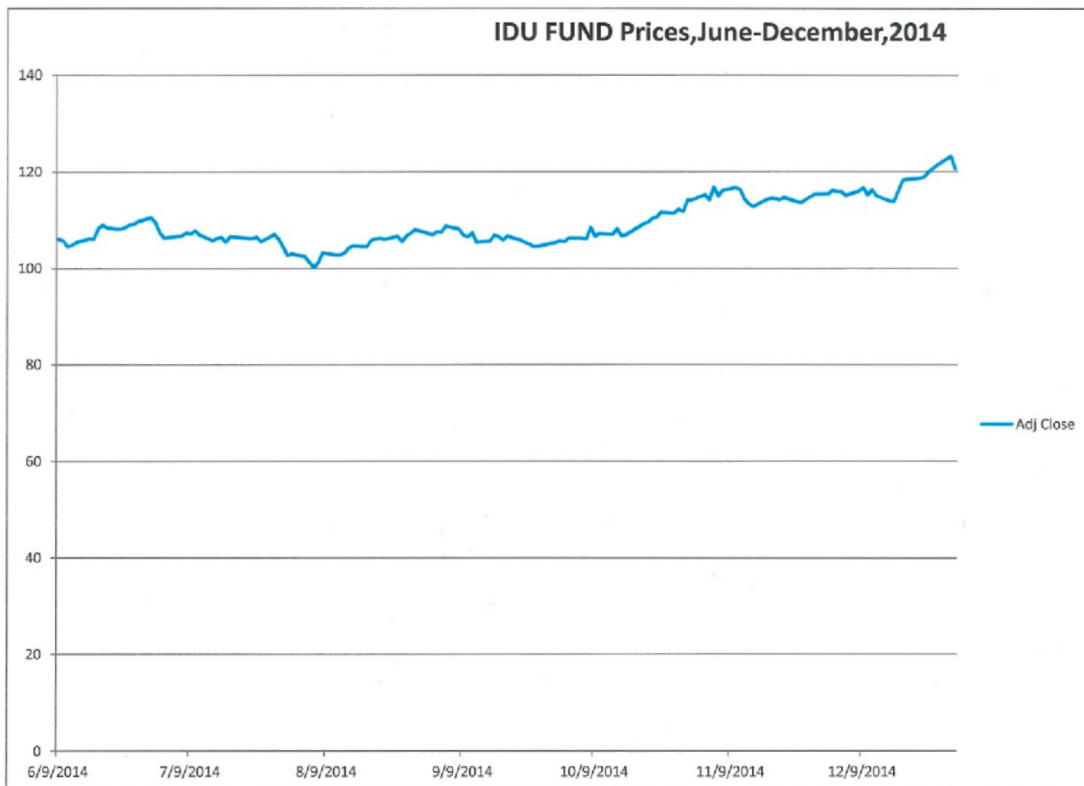
⁹ Yahoo! Finance, <http://finance.yahoo.com/q?s=idu>

¹⁰ Yahoo! Finance, <http://finance.yahoo.com/q?s=idu>

utility stock prices increased in each consecutive month and for the period October-December were significantly higher than the utility stock prices over the period June-July, which was used by Dr. Amit in his Surrebuttal Testimony. This same conclusion is supported by Graph 1 below.

Thus, using the reasoning in the ALJ's Report, the results of the analysis in Dr. Amit's surrebuttal indicate that the ROE is too high for Xcel. However, the Department does not recommend a lower ROE than the 9.64 percent in Dr. Amit's Surrebuttal testimony.

Graph 1: Prices for iShares U.S. Utilities Index Fund (IDU)



Based on the discussion above, Proposed Finding 382 is counter to any reasonable financial analysis and is not supported by any analysis in the record.

Proposed Finding 382 should be amended as follows:

~~382. In this case, however, the Administrative Law Judge concludes that the record shows that the 30-day period used in the Department's Surrebuttal testimony best represents the currently expected future market conditions. ~~may not be representative of the time period in which the ROE will remain in effect.~~ More specifically, the record shows that the dividend yields used in the Department's Surrebuttal Testimony ~~were~~ while significantly lower than the dividend yields used in its Direct Testimony, still represent normal market conditions at that time. ~~falling by 54 and 26 basis points, respectively, from the Department's initial analysis.~~ The lower dividend yields simply reflect the overall upward trend in the stock market valuation. The Department's updated 30-day dividend yields included in its Surrebuttal Testimony appropriately reflect current normal market conditions. ~~These decreased dividend yields were the result of unusually high stock prices during the June July 2014 time period used in the Department's Surrebuttal Testimony. Since that time, utility stock prices have declined relative to the overall stock market and moved more in-line with historic expectations. As a result, the Department's updated 30-day dividend yields included in its Surrebuttal Testimony may reflect a short-term anomaly.~~ ~~{footnotes omitted}~~~~

5. Exception to Proposed Finding 383

Proposed Finding 383 recommends that the Commission use an average of the ROEs recommended by the Department in its Direct Testimony, the 30-day period dividend yield ROE estimated by the Company in its Rebuttal Testimony, and the ROE recommended by the Department in its Surrebuttal Testimony. To support the recommendation, the Report provides the following reasons:

- a. Since the Company proposed a MYRP, it is desirable to minimize the impact of any market anomaly that may have contributed to the variability in the dividend yields.
- b. The Commission took a similar approach (averaging) in the recent MERC rate case.

The Department disagrees with Proposed Finding 383 because it is based on wrong or inappropriate arguments.

First, as explained by the Department,¹¹ MYRP does not increase Xcel's risk because the ROE has the same likelihood of going up or down in 2015.

Second, there is no reason to award Xcel for its choice to file an MYRP as opposed to an ordinary rate case.

Third, as the Department demonstrated in its exception to Finding 382 that no market anomaly existed over the period October, 2014 through December, 2014.

Fourth, as demonstrated by the Department, no unusual variability in the dividend yields existed. The Department explained:¹²

The Company confused the concept of volatility with the concept of trend. Volatility measures changes above and below an average value over a given time period. It does not measure, however, the absolute change in value over a given time period. A commonly used volatility measure, VIX, measures the volatility of the S&P 500. The average VIX over the period October 1, 2013 through October 31, 2013 was 15.41, compared to the average VIX of 11.40 for the period June 7, 2014 through July 7, 2014. Thus counter to Xcel's claim, market volatility went *down*, not up, during the Surrebuttal Testimony period as compared to volatility during the Direct Testimony period [footnote omitted].

Fifth and finally, the finding of facts must be based solely on the record and not on a prior Commission decision regarding a natural gas utility that may reflect significantly different circumstances.

Proposed Finding 383 should be replaced as follows:

~~383. Because the Company has proposed a MYRP and to minimize the potential effect of any market idiosyncrasies that may have contributed to the variability in the dividend yields, the Administrative Law Judge concludes that the authorized ROE should be based on data from more than just the one 30-day period used in the Department's Surrebuttal Testimony. Similar to the approach taken by the Commission in the recent MERC rate case, the Administrative Law Judge recommends that the Commission consider the DCF results from the three~~

¹¹ DOC Reply Br. at 8.

¹² *Id* at 7.

~~most recent 30-day time periods. More specifically, the Administrative Law Judge recommends that the Commission consider the DCF results from: the 30-day period included in the Department's Direct Testimony (covering October 1-31, 2013); the 30-day period included in the Company's Rebuttal Testimony (covering May 1-30, 2014); and the 30-day period included in the Department's Surrebuttal Testimony (covering June 7-July 7, 2014).~~

Based on the record in these proceedings, the Company's proposed MYRP has no impact on the required ROE for Xcel. The 30-day dividend yields calculated by the Department in its Surrebuttal Testimony represent normal market conditions and most appropriately reflect future market condition expectations. Therefore, the 30-day dividend yields calculated by the Department in its Surrebuttal Testimony are the most appropriate dividend yields to be used in a DCF analysis.

6. Exception to Proposed Finding 385

In addition, Proposed Finding 385 states that an ROE of 9.77 percent is more reasonable than 9.64 percent ROE because:

- a. It is confirmed by the 9.85 percent CAPM ROE estimated by the Department in its Surrebuttal Testimony.
- b. It is justified by the Company's need to access the capital market to finance its future substantial capital investment.
- c. A 9.64 percent ROE may send potential investors negative signals because it is in the low end of the ROEs approved since the beginning of 2014.

Based on the record in these proceedings, the Department concludes that the reasons the ALJ provided in recommending a ROE of 9.77 percent instead of 9.64 percent are not reasonable.

First, the ALJ Report recommendation of 9.77 percent is based partially on the Department's 9.80 percent ROE recommendation in its Direct Testimony. The Report then states that its recommendation is confirmed by the Department's 9.85 percent CAPM-ROE in its Surrebuttal Testimony. The Department notes that its CAPM ROE in its Direct Testimony was

9.63 percent.¹³ Thus, using the Report's rationale, the Department CAPM ROE in its Direct Testimony confirms the Department ROE of 9.64 which it recommended in its Surrebuttal Testimony. However, it is not reasonable to compare the results of CAPM and DCF analyses that are conducted at different times.

Second, as the Department explained in its Direct Testimony,¹⁴ using the CAPM involves significant disputed issues. Therefore, the CAPM should be used only to confirm that the contemporaneous DCF results are in the range of reasonableness. It is simply not reasonable to conclude that, because the CAPM result from the Department's Surrebuttal Testimony is closer to the arbitrary average ROE used by the ALJ, the 9.77 percent is more appropriate than the 9.64 percent recommended by the Department in its Surrebuttal Testimony.

Third, the ALJ Report finding that, due to NSP's future substantial capital investment, NSP should be allowed a higher ROE is not supported by the record and is not reasonable. In its Direct Testimony, the Department concluded that, based on well accepted risk measures, NSP is not riskier than Dr. Amit's comparison groups. Therefore, no risk-related DCF ROE adjustment is appropriate.¹⁵ Moreover, as shown in the Department's Surrebuttal Testimony, both the higher equity ratio and the higher bond rating for NSP in comparison with the comparable groups¹⁶ indicate a lower, not higher, risk for NSP. Since both the bond rating and equity ratio reflect NSP's future substantial capital investment, no upward adjustment to the Department's 9.64 recommended ROE is warranted.

¹³ Ex. 400 at 42 (Amit Direct).

¹⁴ Ex. 400 at 38 (Amit Direct).

¹⁵ Ex. 400 at 21-22 (Amit Direct).

¹⁶ Ex. 403 at 12-15 (Amit Surrebuttal).

Fourth and finally, the Report's finding that 9.64 percent ROE would send investors a negative signal is not supported by the record. The 9.64 percent recommended by the Department in its Surrebuttal Testimony appropriately reflects the more current financial and economic environment, according to well accepted financial principles. There existed no market anomalies during the period October, 2013 – July, 2014. The ALJ proposed averaging the ROEs across various time periods is not reasonable because it includes outdated data that misrepresents the most current investor's expectations in the record.

Thus, Proposed Finding 385 should be replaced as follows:

~~385. The reasonableness of a 9.77 percent ROE for the Company is confirmed by other evidence in the record. First, a 9.77 percent ROE is similar to the 9.85 ROE calculated by the weighted CAPM results provided in the Department's Surrebuttal Testimony. In addition, the Company's need to access capital for its substantial capital investment plans strongly suggest that a 9.77 percent ROE is more reasonable than the 9.64 ROE recommended by the Department in Surrebuttal Testimony. A 9.64 percent ROE could send a negative signal to potential investors because it is at the low end of ROEs approved since the beginning of 2014, whereas 9.77 percent reflects the average. For these reasons, the Administrative Law Judge recommends that the Commission adopted a ROE of 9.77 percent, including flotation costs~~

Based on the record in these proceedings, the 9.64 percent ROE is the most reasonable ROE in these proceedings. This ROE would allow the Company to maintain its credit rating and support the Company need to access the capital markets under reasonable terms. Moreover, an ROE of 9.64 percent is sufficient to attract potential investors to invest in the Company.

II. DEPRECIATION AND PLANT RETIREMENTS IN THE 2015 – PASSAGE OF TIME

A. The Report Appropriately Recommends That The 2015 Revenue Requirement Must Recognize Passage of Time Impacts such as Depreciation Attributable to 2014 Capital Additions As Well As Plant Retirements, But Its Calculation Is Not Supported By The Record

The ALJ Report agrees with the Department that just and reasonable rates require consideration not only of the increased costs associated with specific capital projects requested to

be added to rates in 2015, but also passage of time on depreciation and rate base for 2015. In response to discovery, the Department learned that Xcel's 2015 Revenue Requirement request violated long-standing equitable ratemaking principles: it included all of the higher capital costs associated with select new capital projects to be added in 2015 (i.e., the great majority of Xcel's planned 2015 capital projects), but omitted any offsetting (decreasing) adjustments to account for depreciation paid by ratepayers for plant included in the 2014 rate base and related accumulated depreciation for 2015 of \$17.53 million, and retirements of plants included in the 2014 rate base to reflect 2015 retirements of \$0.536 million. The Report states, as follows:

229. Because [traditional ratemaking factors] include consideration of the utility's depreciation expense and rate base, the Administrative Law Judge agrees with the Department that the Commission should consider the effects of the passage of time on depreciation and rate base in determining the 2015 Step revenue requirement. Otherwise, the 2015 Step will not take into account known and measurable changes in depreciation expense, rate base, and accumulated depreciation reserve for non-Step projects placed in to service in 2014, but will only reflect changes due to Step projects. Consideration of the effects due to the passage of time on rate base and depreciation is necessary to ensure just and reasonable rates. [footnote omitted]

Thus, the Department commends these important findings of the ALJ's Report and limits exceptions to the incorrect conclusion that the Company's revised passage-of-time calculation of an \$18.48 million *increase* to 2015 revenue requirements for the 2015 depreciation expense and accumulated depreciation in 2015 is adequately supported, rather than Xcel's previous calculation (used by the Department) of a \$17.53 million *decrease* and related \$0.536 million in retirements for transmission and distribution reduction. Xcel did not adequately support its revision. Thus, the Department takes exception to Proposed Findings 230 – 234.

1. Exception to Proposed Finding 230

Proposed Finding 230 states:

230. A careful review of the record in this case shows that the Department's proposed passage of time adjustments to 2015 Step revenue requirements do not fully account for capital-related effects of the passage of time. The Department's \$17.53 million downward adjustment only reflects the change in accumulated depreciation for non-Step projects placed into service in 2014; it does not reflect the increased expenses due to annualization of depreciation expense or the additions to rate base from these same set of projects. When these additional passage of time components are considered, they more than offset the passage of time reductions recommended by the Department. [footnotes omitted]

The \$17.53 million downward adjustment to reflect the passage of time regarding 2015 rate base was the figure initially provided by Xcel's response to Department follow-up discovery (response to DOC IR 2113)¹⁷ after the Department learned that the Company had not included passage-of-time effects for 2015. Ms. Campbell responded to Ms. Perkett's Rebuttal Testimony in which Xcel criticized the Department's use of Xcel's calculation, and in which Ms. Perkett stated that Xcel did not include the increases in the accumulated depreciation reserve or increases in plant from non-step projects placed in service for 2014, as follows:¹⁸

First, I only had the Company update depreciation for the passage of time for capital projects that were in-service by the end of 2014, since all 2015 Step projects (81.3 percent) were already updated by the Company in their 2015 Step. That is, because Xcel already annualized depreciation expense for the majority of projects, it was not necessary to ask for this information. The remaining 2015 non-step projects (18.7 percent) was not in the Company's revenue requirement proposal for this rate case, so I determined that it was not necessary for Xcel to update the part of the rate case that was not a part of the Company's initial proposal. Second, my understanding of information request no. 2113 is that it requests updating of all depreciation for the passage of time, which would include all changes in depreciation expense and depreciation reserve, as discussed on page 163 and (NAC-32) of my Direct Testimony.

Further, as she testified on cross-examination, Ms. Campbell cannot confirm what assumptions Xcel did or did not include in its revised calculation referenced in Ms. Perkett's Rebuttal

¹⁷ Ex. 429 at 158 and NAC-32 (Xcel response to DOC IR 2113 received on April 16, 2014) (Campbell Direct).

¹⁸ Ex. 435 at 117 (Campbell Surrebuttal).

Testimony at 5-6 and in her Rebuttal Schedule (LHP-2) Schedule 2. For example, in response to questions by Xcel's attorney, Ms. Campbell testified that Ms. Perkett's Schedule 2 page 5 of 6 does not identify the assumptions included in the figures from which Xcel calculated an \$18 million increase, and emphasized that Ms. Perkett's numbers had not been audited or confirmed by the Department.¹⁹

I think I have a hard time saying yes to that [to taking the difference between two particulars numbers on Schedule 2 page 5 of 6 to arrive at the passage of time adjustment] because I have no idea if that depreciation expense, what it represents and if it's parts already in the step, if it's parts in the revenue requirement you didn't ask for. So . . . theoretically maybe yes, but not really because I haven't audited it and *I don't know what that depreciation expense number represents.*

Ms. Perkett's supporting Schedule 2 does not confirm the very statements she makes such as that "additional components for the passage of time adjustment more than offset the reduction to rate base Ms. Campbell recommends"²⁰ or that "[w]hen all elements are considered, the passage of time adjustment would support an increase rather than a decrease to the 2015 Step."²¹ Counsel for Xcel asked Ms. Campbell a series of hypothetical questions about how the Department would calculate a passage of time adjustment.²² Consistent with her quoted response above, Ms. Campbell's point was that Ms. Perkett's Schedule 2 page 5 of 6 did not provide sufficient information to know the assumptions Xcel included in its calculation (no footnote explanations, columns poorly labeled and no supporting work papers) nor had the Department been able to verify or audit those numbers.

For these reasons, the Proposed Finding 230 should be modified, as follow:

¹⁹ Tr.V. 5 at 52-53 (Campbell) (emphasis added).

²⁰ See Ex. 94 at 5 (Perkett Rebuttal).

²¹ *Id.* at 7.

²² Tr.V. 5 at 51-53 (Campbell).

230. A careful review of the record in this case shows that the Department's proposed passage of time adjustments to 2015 Step revenue requirements relies on Xcel's initial response to Department discovery. To the extent Xcel claims that its \$17.53 million downward adjustment does not fully account for capital-related effects of the passage of time, Xcel has not demonstrated the reasonableness of the revised adjustment proposed by Ms. Perkett in her Schedule 2 of her Rebuttal Testimony. [footnote: Ex. 435 at 117 (Campbell Surrebuttal); Tr.V. 5 at 52-53 (Campbell)].~~The Department's \$17.53 million downward adjustment only reflects the change in accumulated depreciation for non-Step projects placed into service in 2014; it does not reflect the increased expenses due to annualization of depreciation expense or the additions to rate base from these same set of projects. When these additional passage of time components are considered, they more than offset the passage of time reductions recommended by the Department. [citation omitted]~~

2. Exception to Proposed Findings 231-233

Proposed Findings 231-234 each rely on Ms. Perkett's unsupported Schedule 2 to her Rebuttal Testimony and, thus, these proposed findings are noted together, below, as follows:

231. In its Reply Brief, the Department questioned whether the \$18.48 million increase in depreciation expense calculated by the Company reflects the incremental increase in depreciation expense beyond that already included in the 2015 Step calculation. The Department asserted that the amount appears to be the full increase in depreciation expense from 2014 to 2015. The evidence demonstrates, however, that the \$18.48 million amount is the incremental increase, not the full amount. [footnote omitted]

232. In an attachment to her testimony, Company witness Ms. Lisa H. Perkett provided a calculation of the increased depreciation expense for the passage of time from 2014 to 2015 excluding 2015 Step projects. This calculation was done to correct an error in the Company's response to Department Information Request No. 2113. This Information Request asked specifically for a calculation of the effect of the passage of time without the 2015 Step projects. As a result, Ms. Perkett's updated calculation also excludes the 2015 Step projects and represents the incremental increase, not the full increase. [footnotes omitted]

233. This conclusion is confirmed by the Rebuttal Testimony of Ms. Perkett. In her Rebuttal Testimony, she calculates the passage of time impact for "non-Step projects placed in service in 2014." "[T]he result is not a \$17.5 million reduction [as claimed by the Department], but a \$1.9 million increase." [footnotes omitted]

234. Based on the foregoing analysis, the Administrative Law Judge concludes that no downward adjustment to the Company's 2015 Step revenue requirement

for the passage of time is necessary. In addition, because the Company has not requested an adjustment for the passage of time, no increase is necessary.

As Ms. Campbell testified on cross-examination, Ms. Perkett's Schedule 2 *does not* show that the \$18.48 million amount is the incremental increase in depreciation expense for capital projects not requested in the 2015 Step. Further, Ms. Perkett's Schedule 2 does not prove that Xcel did not double count amounts already captured in the 2015 Step.²³ As Ms. Campbell testified, since Xcel's 2105 Step already included increases in depreciation expense for both projects placed in service in 2014 to be annualized and for new 2015 projects, all increases in depreciation were already added to the 2105 Step.²⁴ Thus, adding the increased depreciation a second time would double-count such expenses. For the convenience of the Commission, Ms. Perkett's Rebuttal Schedule (LHP-2) Schedule is attached to these Exceptions as Attachment 1 so that readers may easily identify that this schedule does not provide the math or other calculations that would confirm Ms. Perkett's view.

It is also important to keep in mind that whatever amount of capital costs Xcel chose not to include in its 2015 Step and for which Xcel does not request recovery in this proceeding is likely small, as Ms. Campbell testified.²⁵ Xcel requests recovery in 2015 of all but approximately 18.7% of capital projects (100%-81.3%=18.7%).²⁶ The capital cost of that 18.7% of projects is not a figure in the record, although the Company included its (unexamined) 2015 forecasted revenue deficiency for its rate base.²⁷

For these reasons, Proposed Findings 231-34 should be amended, as follows:

²³ Tr.V. 5 at 50-53 and 59-61 (Campbell).

²⁴ Ex. 435 at 117 (Campbell Surrebuttal).

²⁵ Ex. 435 at 114-119 (Campbell Surrebuttal).

²⁶ *Id.*

²⁷ *Id.* at 114-116.

231. In its Reply Brief, the Department questioned whether the \$18.48 million increase in depreciation expense calculated by the Company reflects the incremental increase in depreciation expense beyond that already included in the 2015 Step calculation. The Department asserted that the amount appears to be the full increase in depreciation expense from 2014 to 2015. The evidence does not demonstrates, however, that the \$18.48 million amount is the incremental increase, not the full amount. [footnote omitted]

232. In an attachment to her testimony, Company witness Ms. Lisa H. Perkett provided a calculation of the increased depreciation expense for the passage of time from 2014 to 2015 excluding 2015 Step projects. This calculation was done to correct an error in the Company's response to Department Information Request No. 2113. This Information Request asked specifically for a calculation of the effect of the passage of time by updating of all depreciation for the passage of time for 2015 (except for the 2015 Step projects already reflected in the 2015 Step), which would include all changes in depreciation expense and depreciation reserve, as discussed on page 163 and (NAC-32) of Ms. Campbell's Direct Testimony without the 2015 Step projects. [footnote: Ex. 429 at 163 and NAC-32 (Campbell Direct).] As a result, Ms. Perkett's updated calculation does not show whether it also excludes the 2015 Step projects and represents the incremental increase, not the full increase. [footnotes omitted]

233. This conclusion stated in ~~is confirmed by~~ the Rebuttal Testimony of Ms. Perkett, cannot be verified by her Schedule 2. [footnote: *Id.*; Tr.V. 5 at 52-53 (Campbell).] ~~In her Rebuttal Testimony, she calculates the passage of time impact for "non Step projects placed in service in 2014." "[T]he result is not a \$17.5 million reduction [as claimed by the Department], but a \$1.9 million increase."~~ [citation omitted]

234. Based on the foregoing analysis, the Commission Administrative Law Judge concludes that a passage of time adjustment is reasonable, and that Xcel did not demonstrate that no downward adjustment to the Company's 2015 Step revenue requirement for the passage of time is necessary. The only passage of time adjustment amount supported by this record is the Department's downward adjustment of \$17.53 million and \$0.536 million decrease for transmission and distribution retirements. [footnote: Ex. 450 at 9-11 (Campbell Opening).] In addition, because the Company has not requested an adjustment for the passage of time, no increase is necessary.

III. CHANGES TO IN-SERVICE DATES FOR CAPITAL PROJECTS (2014 AND 2015 STEP)

A. New Capital Projects Not Requested in Xcel's Initial Filing Should Be Excluded From Rates

Although this issue involves relatively small dollars (a revenue requirement reduction of \$2.18 million for 2014 and of \$2.05 million for 2015) and a relatively small number of projects that are delayed to periods outside the test year or step year, it concerns an important ratemaking principle: the Department strongly opposes Xcel's request to recover in rates the costs of capital projects it did not request as part of its initial rate case filing.²⁸ Allowing a utility to substitute costs of newly-identified projects for the costs of initially-requested projects that are discovered to be ineligible for rate recovery during the rate case investigation period would unreasonably burden other parties,²⁹ and would constitute a significant and unwarranted departure from traditional ratemaking. Thus, the Department respectfully takes exception to Proposed Finding Findings 499, 500 and 501.

1. Xcel has not shown that it is reasonable for the Commission to depart from its traditional ratemaking practice of prohibiting a utility from replacing or substituting new costs as other initially requested costs are shown during discovery to be ineligible for rate recovery

Given that this matter is the first multi-year rate filing before the Commission, the Department seeks a clear Commission ruling that, consistent with traditional ratemaking for single test-year rate cases, Xcel is not permitted to swap or replace the costs of new capital projects for the costs of projects initially requested in its initial rate case filing after facts came to light in discovery that certain initially-requested projects are ineligible for rate recovery during the test year and step year at issue in case. Such a departure would unreasonably burden parties

²⁸ Ex. 435 at 102-109 (Campbell Surrebuttal); Ex. 429 at 150-154 (Campbell Direct).

²⁹ Ex. 435 at 104-105 (Campbell Surrebuttal)

and, specifically, public agencies such as the Department which investigates rate cases on behalf of the public.³⁰ Further, such a departure would damage the quality of the record before the Commission.

Based on responses to Department discovery provided in March 2014, it became clear that certain initially proposed capital projects would not be used and useful within the 2014 test year or within the 2015 Step year, contrary to Xcel's initial filing. As Ms. Campbell testified Xcel, like other regulated utilities, has an incentive due to the rate case process to be overly optimistic regarding in-service dates than it may actually meet.³¹ In her Direct Testimony, filed on June 5, 2014, Ms. Campbell recommended denial of cost recovery of capital projects that would not be used and useful during this case. In the July 7, 2014, Rebuttal Testimony of Ms. Perkett and Mr. Clark,³² Xcel opposed the Department's recommendation of denial and affirmatively requested that rates include the costs of new substitute or replacement projects that the Company had not included in its initial rate case filing but that Xcel stated would be used and useful during the timeframes applicable in this rate case.

Allowing utilities to swap new costs and expenses for those initially identified in its rate case filing is unreasonable; it would effectively allow a utility a rolling opportunity to amend its initial rate case request without a reciprocal discovery opportunity for other parties to examine the new requests.³³ Moreover, parties' significant early discovery efforts would be rendered moot if new cost items were to be allowed to replace the costs of initially-requested items. Adopting Xcel's proposed departure from the Commission's traditional ratemaking practice

³⁰ Ex. 435 at 105 (Campbell Surrebuttal).

³¹ Ex. 450 at 8 (Campbell Opening).

³² Ex. 94 at 39-42 (Perkett Rebuttal); Ex. 100 at 12-19 (Clark Rebuttal)..

³³ Ex. 435 at 102-109 (Campbell Surrebuttal).

would unreasonably prejudice parties' abilities to investigate the reasonableness of initially proposed projects as well as later-proposed costs and expenses. Further, the record before the Commission would lack the results of such investigations.

2. The Report reasonably concluded that the 2014 test year and 2015 Step should be based on the most current in-service dates for capital projects and that projects delayed beyond those timeframes are not eligible for rate recovery

The Department agrees with the Report's conclusions identified in Proposed Findings 496 and 498 that the most current in-service dates for capital projects must be used for the 2014 test year and 2015 Step, and that projects delayed beyond those timeframes are not eligible for rate recovery, as follows:

496. Based [on] this standard, the Administrative Law Judge concludes that the 2014 test year and 2015 Step should be based on the most current in-service dates for capital projects because otherwise the rates will include recovery of costs for projects that are not "used and useful."

498. In addition, while the Administrative Law Judge recognizes that the utility industry is a dynamic business and priorities change, the utility still has a legal obligation to demonstrate that its test year rate base and depreciation expense include projects that are used and useful. Projects that have been delayed do not meet this standard. [footnote omitted]

The Department, however, questions how the proposed compromise identified in Proposed Finding 499 would be implemented within the limited timeframes and opportunity for testimony subsequent to rebuttal testimony in rate cases. While an after-the-fact approach based on an idea similar to this compromise may be developed for future rate cases, the record in this proceeding does not support the rationale identified in Proposed Finding 500 or the ultimate conclusion provided in Proposed Finding 501.

3. Exception to Proposed Finding 499

Proposed Finding 499 states:

499. With regard to the Company's proposal that it be allowed to substitute replacement projects from capital projects that have been delayed, the Administrative Law Judge concludes that the Company should only be allowed to substitute replacement projects when: (1) the Company has shown that the replacement projects are necessary, the costs are prudent, and the projects will be in-service during the test year; and (2) the other parties have had sufficient time to review the proposed replacement projects. The Administrative Law Judge concludes that such an approach is a reasonable compromise between the Company's position and the Department's position because it recognizes that a utility's capital plans are bound to change somewhat during the course of a long MYRP proceeding but also holds the Company to its burden of proof. [footnote omitted]

The Department appreciates the Report's attempt to broker a compromise, but concludes that this well-intended approach would not be consistent with the ratemaking concept of a test year or the procedures in rate cases. Investigating a new utility proposal in rebuttal testimony would not be feasible since typically there is not time for even one round of discovery to be issued between rebuttal and surrebuttal testimonies, given that the goal at that point in the proceeding is to narrow issues, not expand them and given the typical number of issues that typically need to be addressed.

Limiting the time for parties to investigate new proposals late in the proceeding, as occurred in this rate case, would effectively shift to parties other than Xcel a burden to start over in their discovery efforts to essentially "disprove" the reasonableness of costs of projects not requested in the Company's initial rate case filing. As the Minnesota Supreme Court held in *In re NSP*, at no time in a rate case proceeding do parties other than Xcel bear a burden of proving the reasonableness of costs proposed by the Company.³⁴

If the Commission wishes to discuss future changes to its rate-case procedures, a proposal could be developed to ensure that "1) the Company has shown that the replacement projects are

³⁴ *In re NSP*, 416 N.W.2d 719 at 723, 725-26 (Minn. 1987).

necessary, the costs are prudent, and the projects will be in-service during the test year; and (2) the other parties have had sufficient time to review the proposed replacement projects.” However, based on the procedures used in this rate case, the Department concludes that it would not be reasonable to grant Xcel recovery of costs that could not feasibly be investigated in this proceeding.

Proposed Finding 499 should be amended as follows:

499. With regard to the Company’s proposal that it be allowed to substitute replacement projects from capital projects that have been delayed, the Administrative Law Judge concludes that the Company should only be allowed to substitute replacement projects when: (1) the Company has shown that the replacement projects are necessary, the costs are prudent, and the projects will be in-service during the test year; and (2) the other parties have had sufficient time to review the proposed replacement projects. [citation omitted]. The Administrative Law Judge concludes that such an approach is a reasonable compromise between the Company’s position and the Department’s position because it recognizes that a utility’s capital plans are bound to change somewhat during the course of a long MYRP proceeding but also holds the Company to its burden of proof. However, in this proceeding, the Commission concludes that Xcel did not meet its burden of proof to show that the replacement projects are necessary and the costs are prudent.

4. Exception to Proposed Finding 500

Proposed Finding 500 states:

500. In Rebuttal Testimony, Company witness Lisa H. Perkett identified certain substitute projects for the 2014 test year. Inclusion of these projects would appear to decrease the Department’s proposed revenue reduction from \$2.18 million to \$1.8 million for changes to in-service dates in 2014. No party disputed the need for these specific substitute projects or the costs. The Department, however, disputed the propriety of including substitute projects generally on the grounds that such projects would not be subject to adequate review by the parties. While ensuring the parties have adequate time to review the proposed new projects is important, in this case, the Department was provided the list of substitute projects on March 21, 2014 in response to an Information Request and these same projects are included in Ms. Perkett’s Rebuttal Testimony filed in June 2014. [footnote omitted].

The above proposed finding is of concern for three main reasons. First, in Minnesota utility ratemaking, even if a party other than the requesting utility does not rebut a claimed cost, the utility enjoys no right to a finding of reasonableness by default.³⁵ The *In re NSP* Court specifically rejected Xcel's (NSP's) argument that in a rate case "if the utility supplies evidence to support an issue and no, or insufficient, evidence is presented to rebut the utility's position, an un rebuttable presumption arises to meet the burden of proof and requires a finding favorable to the utility as a matter of law." *Id.*

Second, the Department does not know and the record does not reflect which of the new replacement projects are in fact needed and whether or not the costs of all of the replacement projects are reasonable. The Department agrees that utilities capital plans are likely to change over the course of time which is why Ms. Campbell issued discovery to require Xcel to identify changes to the in-service dates and costs for capital projects the Company included in its initial rate case filing. Xcel has an incentive in a rate case to over forecast the extent to which planned capital projects are likely to be completed and, thus, be used and useful to ratepayers.³⁶ Knowing this incentive, the Department undertook reasonable discovery to verify the eligibility of Xcel's initially-proposed projects.³⁷ It is noteworthy that Xcel responded only when asked in discovery (it did not otherwise volunteer) that some of its capital projects likely would not be used and useful to ratepayers within the timeframes represented to the Commission in Xcel's initial filing.³⁸

³⁵ *In re NSP*, 416 N.W.2d 719 at 723, 725-26 (Minn. 1987).

³⁶ Ex. 435 at 104 (Campbell Surrebuttal); *see* Ex. 429 at 112 (Campbell Direct).

³⁷ Ex. 435 at 105 (Campbell Surrebuttal).

³⁸ *See* Ex. 429 at 150-153 (Campbell Direct).

Third, with all due respect, the Department is troubled by the suggestion that having received a discovery request on March 21, 2014, it had adequate time to engage in new discovery as to the large number of substitute capital projects and to complete its Direct Testimony by June 5, 2014. Unfortunately, this particular issue was one of many important, unresolved issues still subject to the Department's discovery efforts and examination, and the detailed and lengthy Direct Testimony of Ms. Campbell (177 pages of text alone) evidences the considerable challenges faced by the Department in investigating this multi-year rate case.

For these reasons, Proposed Finding 500 should be deleted, as follows:

~~500.—In Rebuttal Testimony, Company witness Lisa H. Perkett identified certain substitute projects for the 2014 test year. Inclusion of these projects would appear to decrease the Department's proposed revenue reduction from \$2.18 million to \$1.8 million for changes to in-service dates in 2014. No party disputed the need for these specific substitute projects or the costs. The Department, however, disputed the propriety of including substitute projects generally on the grounds that such projects would not be subject to adequate review by the parties. While ensuring the parties have adequate time to review the proposed new projects is important, in this case, the Department was provided the list of substitute projects on March 21, 2014 in response to an Information Request and these same projects are included in Ms. Perkett's Rebuttal Testimony filed in June 2014. [footnote omitted].~~

5. Exception to Proposed Finding 501

Proposed Finding 501 states:

501. Based on the evidence in the record and for the reasons discussed above, the Administrative Law Judge recommends that the Commission reduce the Company's proposed 2014 test year revenue requirement and 2015 Step test year revenue requirement to reflect the updated in-service dates for projects included in the Company's initial filing, but also allow the substitution of the projects specified by Company witness Ms. Perkett in her Rebuttal Testimony. [footnote omitted]

This proposed finding simply states the Report's conclusion which, for the reasons explained above, must be rejected in this matter.

For the reasons discussed above, Proposed Finding 501 should be amended, as follows:

501. Based on the evidence in the record and for the reasons discussed above, ~~the Administrative Law Judge recommends that~~ the Commission reduces the Company's proposed 2014 test year revenue requirement and 2015 Step test year revenue requirement to reflect the updated in-service dates for projects included in the Company's initial filing, but does not also allow the substitution of the projects specified by Company witness Ms. Perkett in her Rebuttal Testimony. [footnote omitted]

IV. QUALIFIED PENSION EXPENSE DISCOUNT RATE (ISSUE 4) AND 2008 MARKET LOSS (ISSUE 5).

A. Introduction

It is with some hesitation that the Department files exceptions to the Report's recommendation to adopt Xcel's positions both as to the discount rate to use for ratemaking purposes for the XES Pension Plan,³⁹ and with respect to Xcel's proposed recovery in 2014 rates of its 2008 Market Loss.⁴⁰ Xcel's qualified pension is an important employee benefit that the Department strongly supports.⁴¹ The importance of this issue to Company employees as well as to ratepayers cannot be overstated. The Commission in other recent rate cases expressed its intention to open a generic docket to examine how test-year pension expense should be set for

³⁹ Xcel proposes to use a lower discount rate for its XES plan than it uses for its Expected Return on Assets (EROA) while it uses the same discount rate as the EROA for its NSPM pension plan. Only the discount rate for the XES plan is a disputed issue in this matter.

⁴⁰ Proposed Findings 124-128 (discount rate), 146-158 (2008 Market Loss) and 168-169 (alternative proposals).

⁴¹ Department supports inclusion in rates amounts to sums adequate for reasonable salaries and benefits to utility employees; such reasonable costs are necessary in the provision of utility service. It does not support, however, paying costs that appear to overstate the test year compared to actual costs in past years, or paying costs that are established by inappropriate or unreasonable assumptions for purposes of setting rates. Ex. 429 at 99 (Campbell Direct). The utility bears the burden of establishing the reasonableness of such costs; any doubt must go to the ratepayers. Minn. Stat. § 216B.03. Because Xcel seeks recovery from ratepayers of 100 percent of its qualified pension benefit costs, particular attention to the reasonableness of the Company's proposed test-year pension expense is warranted.

purposes of ratemaking to ensure that rates include reasonable sums for purposes of funding pension benefits as well as to ensure that utilities are not unfairly over-compensated by ratepayers. The Department looks forward to participating that pension docket which will require, in the Department's view, involvement of independent pension accounting and pension funding experts, due to the complexity of the issues.

The Department does not propose that ratemaking mirror either financial reporting requirements or pension funding requirements,⁴² because the purpose of ratemaking and Minnesota law (such as actual income taxes compared to imputed income taxes) does not mirror either such requirement. It will be helpful to understand the purposes and limitations of these various standards as well as their application (or not) to regulated utilities so that they may be guidelines for ratemaking purposes and can be tailored to serve the Commission's important goal of ensuring that rates are just and reasonable.

Ratemaking is based on reasonably representative values, which typically requires a longer perspective that considers a broad range of factors and influences, including the perspective that it is in the public interest for rates to be set to allow the utility to be financially viable in the long run, under reasonable management of the utility.⁴³ Once placed into effect, such rates do not change until the utility chooses to file a rate petition typically to increase rates or (rarely) the Commission reduces a utility's rates. Assumptions used for financial accounting statements, in contrast, are short-term, point-in-time figures that change annually (or more

⁴² Ex. 429 at 132 (Campbell Direct) (“[I]t is important not to simply tie Xcel’s required pension contribution to a direct pension expense for which ratepayers must pay.”)

⁴³ Ex. 429 at 103 (Campbell Direct).

frequently), similar to pension funding under ERISA, as the Company's financial circumstances change (which does not occur for ratemaking unless the company files a rate case).⁴⁴

B. THE SAME DISCOUNT RATE AND EXPECTED RETURN ON ASSETS (EROA) RATE SHOULD BE USED FOR THE SAME PERIOD OF TIME

The Department continues to recommend that the discount rate for the XES pension plan be increased from 4.74 percent to 7.25 percent so that these two rates, covering the same period of time, are equal -- just as under the Company's NSPM pension plan.⁴⁵ In her Opening Statement, Ms. Campbell summarized the reasons for the Department's recommendation that the same time period (for pension assets and pension liability) calls for the same rates, therefore, the discount rate expected returns on assets and (EROA) rate should be the same and the EROA rate is the reasonable rate to select for both rates in this rate case.⁴⁶

Second, the discount rate [for XES pension plan] is artificially low because it relies on a point-in-time measurement, as the Company acknowledged. By contrast, the NSPM pension account appropriately relies on a longer-term perspective [for its discount rate consistent with its EROA rate]. DOC Ex. 429 at 116 (Campbell Public Direct).

Third, I note in the 12-961 Xcel rate case that the Company was already setting the discount rate and EROA at the same rates for the Aggregate Cost Method (ACM) for the NSP pension plan, so the Department realized that using the same rates made sense and questioned whether Xcel had shown it was reasonable to use different rates for the XES plan. DOC Ex. 429 at 82-83 (Campbell Public Direct).

Fourth, I note that the time period for the EROA (which is used to inflate the value of pension assets to future years when the retirees will retire) and the discount rate (used to determine in today's dollars the pension obligation liability when the retiree is retiring in future years) is for the same time period; it is not reasonable for ratemaking purposes to use different rates that reflect the same time period. Using a lower discount rate artificially overstates pension expense for purposes of ratemaking and is therefore unreasonable. DOC Ex. 429 at 117 (Campbell Public Direct).

⁴⁴ *Id.* at 102-103.

⁴⁵ Ex. 429 at 116-117 (Campbell Direct); Ex. 450 at 5 (Campbell Opening).

⁴⁶ Ex. 450 at 5 (Campbell Opening).

Moreover, Ms. Campbell noted that Xcel's bond study that underlies its proposed discount rate assumption of 4.74 percent was selected by Xcel rather than by an independent actuary as shown on the actuary certificate,⁴⁷ and was not independent of the Company.⁴⁸

1. EXCEPTION TO PROPOSED FINDING 126

Proposed Finding 126 states, as follows:

126. As a result, the Administrative Law Judge reaches a different conclusion in this case. The record in this case demonstrates that both FAS 87 and the ACM are designed to ensure accurate reporting of pension expense but use different methodologies. For that reason, use of the FAS 87 bond-matching discount rate will help ensure that the XES Plan, which is subject to FAS 87, is fully funded. In addition, the record demonstrates that the Company's calculation of its FAS 87 discount rate was based on objective criteria and is similar to the rates used by other utilities. Finally, as the Company noted, if the discount rate had been equal to the EROA since the inception of the XES Plan, customers would have paid more in pension expense through the years because the service cost and interest cost elements of the FAS 87 calculation would have been higher. For these reasons, the Administrative Law Judge concludes the use of the FAS 87 discount rate is more reasonable than use of the EROA rate as the discount rate for the XES Plan. [footnote omitted]

The Department does not agree that the record supports a conclusion that “use of the FAS 87 bond-matching discount rate will help ensure that the XES Plan, which is subject to FAS 87, is fully funded,” or that Xcel used objective criteria that was not dependent on the Company's assumptions.

The Department shares the Commission's goal that Xcel be provided sufficient monies in rates to enable it to meet its funding requirements. Further, the Department shares the goal that employees should be fairly compensated. However, the actual amount of money that Xcel places into its pension fund may not be affected by the Commission's use of the FAS 87 accounting standard to set the discount rate for the XES pension plan (unless the Commission had a specific

⁴⁷ Ex. 429 at 112-113 (Campbell Public Direct).

⁴⁸ Ex. 450 at 5 (Campbell Opening).

requirement for Xcel's pension fund). FAS 87 is an accounting standard for financial statement purposes. Absent a Commission order that requires the approved test-year pension expense to be contributed directly to Xcel's pension funds each year that the discount rate is in effect, Xcel has the discretion to use its rate case pension dollars however it chooses, as long as it complies with its separate pension funding requirements under ERISA. Moreover, as Xcel's own pension witness testified, the "pension funding" method of accounting is the ACM accounting method that Xcel uses for its NSPM pension plan⁴⁹ and for which the discount rate and the EROA are equal to each other (here, 7.25 percent).

Xcel's testimony in this matter does not develop the record as to how much money Xcel will contribute to its pension fund – instead, the great majority of its testimony is concerned on pension accounting with very little focus on Xcel's actual pension funding requirements under ERISA.⁵⁰ Nonetheless, so much of Xcel's testimony and post-hearing briefs read as if the Company's proposed test-year pension expense directly impacts the Company's pension funding, which it simply does not do. The Company liberally used funding-related terms such as "fund," "funding," "unfunded liability," "funding obligation," etc.⁵¹ without clarifying that the context of the testimony was annual pension accounting/reporting methods rather than pension contributions or funding.

The Department appreciates that the Report makes no proposed finding as to whether current ERISA funding requirements dictate that Xcel use a discount rate based on corporate bond yields rather than the EROA. Comments may be helpful, though, concerning Xcel's

⁴⁹ Mr. Schrubbe adopted Mr. Moeller's Direct Testimony that states, "[T]he NSPM pension plan (NSPM Plan) follows a funding method of accounting known as the Aggregate Cost Method (ACM)." Ex. 81 at 6 (Moeller Direct).

⁵⁰ See generally, Ex. 81 (Moeller Direct); Ex. 83 (Schrubbe Rebuttal); Ex. 84 (Wickes Rebuttal).

⁵¹ Ex. 81 at 6 (Moeller Direct).

argument made for the first time in its Reply Brief, and contrary to its own witness testimony that the ACM method is the “pension funding” method (using the EROA rate to equal the discount rate), that ERISA was amended in 2006 to require the discount rate be established according to a corporate bond yield curve, not the EROA.⁵² The Department’s limited review of the ERISA section identified by Xcel, “*see* 29 U.S.C. § 1083(h)(2)(C),” suggests that for some pension plans a corporate bond yield curve that is determined by the Secretary of the Treasury is the measure to be used for the pension funding discount rate. This section of ERISA also appears to now allow a discount rate to be set based on a 25-year average of the Treasury’s corporate bond yields.⁵³ Clearly, ERISA may include flexibility in funding requirements for pension funds that may be quite different from FAS 87 or ACM accounting methods. No Xcel witness testified with specificity as to ERISA funding requirements or as to Xcel’s particular funding requirements under ERISA based on facts specific to Xcel.

Ms. Campbell’s reference to ERISA pension funding requirements in her Direct Testimony was for the purpose of supporting her recommendation -- for ratemaking purposes -- that the same rate should be used for the same period of time. She also believed that ERISA required use of the EROA for funding purposes. She relied on a 2004 American Academy of Actuaries document entitled, “Fundamentals of Current Pension Funding and Accounting for Private Sector” for the proposition that for pension funding, like the NSPM plan, ERISA used the EROA as to the discount rate, which is what the Department recommended for ratemaking purposes. In doing so, she concluded that rates set by using the same rates for the same time

⁵² Xcel Reply Brief at 54. The Report notes Xcel’s position in Proposed Finding 121.

⁵³ 29 U.S.C.A § 1083(h)(2)(C)(iv)(I).

period, and specifically using the EROA rate of 7.25 percent for the discount rate in this case, would not have a negative impact on Xcel's funding under ERISA.⁵⁴

Xcel's actuary witness, Mr. Wickes, provided no testimony to the effect that Ms. Campbell was in error regarding ERISA funding methodology generally or as to Xcel, specifically, nor did Xcel witness Mr. Schrubbe. Xcel witnesses were silent in this regard. That silence is unfortunate for purposes of the record in this matter. Based on the current record, no material weight should be accorded Xcel's new information that was provided for the first time in its Reply Brief and was not subject to cross-examination.

Finally, as to its bond-matching study, Xcel did not show that its assumptions were independent of the Company.⁵⁵ The question is not whether Xcel performed its study correctly, but whether the study itself unfairly favors the Company or is otherwise not independent of Xcel. In this case it is clear that Xcel, not the actuary, determined the discount rate assumptions. Given Xcel's past attempt during a rate case to manipulate its discount rate, the issue of independent assumptions is particularly important, as Ms. Campbell testified, in relevant part:

Sixth, my experience as an auditor is that actuaries' primary concerns are with the understatement of pension expense, not the overstatement of pension expense. This fact points out another reason why reliance on financial accounting data is not appropriate for ratemaking purposes. DOC Ex. 435 at 77 (Campbell Surrebuttal)

Seventh, in response to the concern of using an average discount rate, I noted that in the 12-961 Xcel rate case E002/GR-12-961, the Company attempted to further reduce its discount rate in Rebuttal Testimony and then did a three year average discount rate calculation that resulted in a very small adjustment. In my Surrebuttal Testimony on page 52-53 in the prior rate case, I raised concerns with the Company manipulating its test-year pension expense by adjusting its own assumptions. DOC Ex. 435 at 83 (Campbell Surrebuttal)

⁵⁴ Ex. 450 at 6 (Campbell Opening).

⁵⁵ Ex. 450 at 4-5 (Campbell Opening).

* * *

Ninth, I noted that assumptions used by the Company in calculating pension expense were not independently determined, but rather were selected by the Company, as stated on the Towers Watson actuarial certificate. DOC Ex. 429 at 112-113 (Campbell Public Direct). This is an important point because despite the Company indicating that it is using “actual pension expense” as noted by Mr. Schrubbe in his opening statement, the “actual pension expense” is a calculation that is based on a point in time and with assumptions that are not independent of Xcel. In several rate cases the Department and Commission have recognized that because GAAP accounting (such as FAS 87) is capturing pension expense at a point in time and, therefore, tends to reflect ups and downs of the market and discount rates, it is generally not appropriate for setting rates. DOC Ex. 435 at 80-81 (Campbell Public Surrebuttal).

For the reasons discussed above, Proposed Finding 126 should be amended, as follows:

126. ~~As a result, the Administrative Law Judge reaches a different conclusion in this case. —~~ conclude that ~~the record in this case demonstrates that both FAS 87 and the ACM are designed to ensure accurate reporting of pension expense but use different methodologies. For that reason, use of the FAS 87 bond matching discount rate will help ensure that the XES Plan, which is subject to FAS 87, is fully funded. In addition, the record demonstrates that the Company's calculation of its FAS 87 discount rate was based on objective criteria and is similar to the rates used by other utilities. Finally, as the Company noted, if the discount rate had been equal to the EROA since the inception of the XES Plan, customers would have paid more in pension expense through the years because the service cost and interest cost elements of the FAS 87 calculation would have been higher. For these reasons, the Administrative Law Judge concludes the use of the FAS 87 discount rate is more reasonable than use of the EROA rate as the discount rate for the XES Plan.~~ For ratemaking purposes until the next rate case, and in order for the Commission to examine pension ratemaking issues more closely in a generic docket, the Commission concludes that it is reasonable to use the same discount rate as the EROA rate because the rates cover the same period of time for pension assets and pension liabilities. Therefore, for the XES plan, as for the NSPM plan, the Commission will use a discount rate of 7.25 percent which is equal to the EROA rate.

2. Exception for clarification to Proposed Finding 104

As part of the Background discussion, the Report includes Proposed Finding 104, which states as follows:

104. At a high level, both the ACM and FAS 87 attempt to determine the present value of future benefits and estimated earnings in the pension trust that have accumulated to determine the unfunded obligation. The present value of this unfunded obligation and the current-period earned value are the basis for determining the current- period pension expense accrual. Thus, both the ACM and FAS 87 are affected by the discount rate and rate-of-return assumptions. In addition, as discussed above, both methods provide for a smoothed recognition of unrealized gains and losses in plan asset earnings, such that the level of expense will change more gradually. [footnote omitted]

The Department requests that reference be added to 1) make clear that ACM and FAS 87 are accounting standards for financial reporting and are not actual pension funding requirements, and 2) clarify that the pension liability is calculated with the discount rate while the rate of return assumptions (EROA) are used to calculate estimated pension earnings on the pension assets. Thus, the Department requests the following changes for purposes of accuracy and clarification to Proposed Finding 104:

104. At a high level, both the ACM and FAS 87 attempt for financial reporting purposes and not pension funding purposes to determine the present value of future benefits and estimated earnings in the pension trust that have accumulated to determine the unfunded obligation. The present value of this unfunded obligation and the current-period earned value are the basis for determining the under or overfunded status of the pension fund, which is a component of the current- period pension expense accrual. Thus, both the ACM and FAS 87 accounting methods use ~~are affected by~~ the discount rate to calculate the pension liability and both methods use the expected return on assets or EROA assumptions to calculate estimated pension earnings. [footnote: Ex. 429 at 131-132 (Campbell Direct)] In addition, as discussed above, both methods provide for a smoothed recognition of unrealized gains and losses in plan asset earnings, such that the level of expense will change more gradually. [footnote omitted]

3. Exception for clarity to Proposed Finding 113

Proposed Finding 113 states:

113. The Company's calculation of the pension expense for the XES Plan uses the discount rate provided by FAS 87, the accounting method prescribed for the XES Plan. The primary source for the discount rate is a bond-matching study that is performed as of December 31 of each year. The study includes a matching bond for each of the individual projected payout durations within the plan based on projected actuarial experience. The bonds used in the study must meet certain well- established criteria, and the Company employs numerous tests to validate the reasonableness of the discount rate produced by the bond-matching study. [footnotes omitted]

The Department requests that reference be added to make clear that the bond-matching study performed by Xcel for the XES Plan was not selected or performed independent of the Company and, in particular, this pension discount rate assumption was not selected by an independent actuary.⁵⁶ Thus, the Department requests the following changes for purposes of accuracy and clarification the following changes for purposes of accuracy and clarification to Proposed Finding 113:

113. The Company's calculation of the pension expense for the XES Plan uses the discount rate provided by FAS 87, the accounting method prescribed for the XES Plan. The primary source for the discount rate is a bond-matching study that is performed by the Company as of December 31 of each year. The study includes a matching bond for each of the individual projected payout durations within the plan based on projected actuarial experience. The study was selected and performed by Xcel rather than by an independent entity or actuary. [Ex. 429 at 112-113 and NAC-22 (Campbell Direct) (actuarial certificate stating that Xcel selected assumptions)]. The bonds used in the study must meet certain well-established criteria, and the Company employs numerous tests to validate the reasonableness of the discount rate produced by the bond-matching study. [footnotes omitted]

B. 2008 Market Loss (2014)

Regarding Xcel's 2008 market loss, the Department continues to recommend recovery from ratepayers of 50 percent of the \$12.1 million 2008 market loss recommended by the

⁵⁶ Ex. 429 at 112-113 and NAC-22 (Campbell Direct).

Company, or specifically \$6,032,000.⁵⁷ The Department disagrees that it is reasonable to impose on ratepayers 100 percent of this extreme amount of \$12.1 million for a 2008 market loss of \$19.9 million pension expense in 2014.⁵⁸

Most troubling is that after six years and in light of tremendous recovery of the financial markets, there is still a “2008 market loss” without a material offsetting market gain that one would expect based on recovery of financial market above 2007 financial market levels. The record does not demonstrate a reasonable basis for Xcel’s pension fund to have so significantly underperformed that the Company still proposes to charge its ratepayers such a large percentage of the 2008 market loss (over 60 percent) in the Company’s proposed 2014 increase in pension expense.⁵⁹ Xcel’s ratepayers pay for 100 percent of Xcel’s qualified pension benefit; continuing to require additional ratepayer funding so long after this extraordinary event, is not reasonable.⁶⁰

1. Exception to Proposed Findings 149-151

Proposed Findings 149-151 state, as follows:

149. That additional information requested by the Commission and the other evidence in the record demonstrate that the Company's proposed treatment of gains and losses, including the 2008 Market Loss, in calculating its test year qualified pension expense is reasonable. The record shows the Company's treatment of the 2008 Market Loss is consistent with the Company's long standing practice of including both market gains and losses in its calculation of the pension expense. While this approach results in a significant pension expense in the 2014 test year, ratepayers have received much more substantial benefits from this approach in prior years. As the Company demonstrated, the cumulative benefit to customers of recognizing both gains and losses has been approximately \$332 million on a Minnesota jurisdictional basis from 2000 to 2014. [footnote omitted]

⁵⁷ Ex. 450 at 6 (Campbell Opening).

⁵⁸ See Proposed Findings 150-158.

⁵⁹ Ex. 450 at 6 (Campbell Opening).

⁶⁰ See *id.* at 6-7.

150. In addition, as a result of recognizing pension asset earnings and losses, the pension expense recovered in rates has historically been well below the Service Cost (the actual cost of providing the pension benefit to Company employees). For example, as shown in the figure below, for the NSPM Plan, the pension expense has been below the Service Cost in every year since 2000. [Table 2 omitted][footnote omitted]

151. These facts demonstrate that the Company's approach fairly allocates both the gains and the losses to ratepayers.

The Department respectfully observes that Xcel's claims of recognizing pension asset "earnings and losses" or "gains and losses" over time begs the critical question, "Where are the market gains?" Present market gains clearly should be significant to offset a significant amount of the 2008 market losses. They do not. Instead, Xcel claims essentially that it is reasonable for ratepayers to pay as if they must generate the market gains that Xcel's management did not. The Company has not shown it is reasonable for Xcel to continue to impose 100 percent of the 2008 market loss on ratepayers.

For these reasons, Proposed Findings 149-151 should be changed as follows:

149. That additional information requested by the Commission and the other evidence in the record demonstrate that the Company's proposed treatment of gains and losses, including the 2008 Market Loss, in calculating its test year qualified pension expense is not reasonable. The record shows the Company's treatment of the 2008 Market Loss is consistent with the Company's long standing practice of including both market gains and losses in its calculation of the pension expense, but it does not demonstrate reasonable grounds for Xcel to have experienced so little recovery (i.e. offsetting market gains) in the value of its pension asset during the recent, significant market recovery. ~~While this approach results in a significant pension expense in the 2014 test year, ratepayers have received much more substantial benefits from this approach in prior years. As the Company demonstrated, the cumulative benefit to customers of recognizing both gains and losses has been approximately \$332 million on a Minnesota jurisdictional basis from 2000 to 2014.~~

150. In addition, as a result of recognizing pension asset earnings and losses, the pension expense recovered in rates has historically been well below the Service Cost (the actual cost of providing the pension benefit to Company employees). For example, as shown in the figure below, for the NSPM Plan, the pension expense has been below the Service Cost in every year since 2000.

[Table 2 omitted] This fact, however, does not relieve Xcel of the obligation to demonstrate that it was reasonable for Xcel to have experienced so little recovery in the value of its pension asset during the recent, significant market recovery.

151. These facts do not demonstrate that the Company's approach fairly allocates both the gains and the losses to ratepayers.

2. Exception to Proposed Findings 152-153

Proposed Findings 152-153 state:

152. In addition, the Administrative Law Judge concludes that none of the grounds set forth by the Department provide a reasonable basis for reducing the amount of the 2008 Market Loss reflected in the 2014 test year expense.

153. The Department's argument that the Company's approach is not symmetrical fails to recognize the benefit to ratepayers of having the gains offset pension expense both at the time of the gain and in the future by returning any excess to the pension fund. It would be inequitable to recognize the gains, but not the losses, in calculating the Company's pension expense for ratemaking purposes.

Ms. Campbell addressed the asymmetry of Xcel's 2008 market loss proposal, in the last Xcel rate case, 12-961, and this current case. Her point is that rates increase when pension expense is positive, but rates never decrease when pension expense is negative. Rather, pension expense is assumed to be \$0, and thus ratepayers do not benefit when pension assets are higher than expected pension payouts over time; instead, the additional monies simply remain in the pension plan to offset future pension costs with no refund to ratepayers.⁶¹ Given that asymmetry, the Department urged a longer-term approach to allow the pension funds to recover.⁶²

Additionally, contrary to the Company's claim that it includes both market gains and market losses, and despite the financial market returning to above 2007 levels, the Company has

⁶¹ Ex. 435 at 91 (Campbell Surrebuttal); Ex. 450 at 7 (Campbell Opening).

⁶² *Id.*

not included material market gains to offset material market losses as expected based on recent financial market performance.

For these reasons, Proposed Findings 152-153 should be changed, as follows:

~~152. In addition, the Administrative Law Judge concludes that none of the grounds set forth by the Department provide a reasonable basis for reducing the amount of the 2008 Market Loss reflected in the 2014 test year expense.~~

153. The Department's argument that the Company's approach is not symmetrical is correct in that Xcel's approach allows rates to increase when there is positive pension expense but not to decrease when pension expense is negative. Additionally, contrary to the Company's claim that it includes both market losses and market gains, and despite the financial market returning to above 2007 market levels, the Company has not included material market gains to offset material market losses, as expected based on recent financial market performance. to fails to recognize the benefit to ratepayers of having the returning any excess to the pension fund. It would be inequitable to recognize the gains, but not the losses, in calculating the Company's pension expense for ratemaking purposes.

3. Exception to Proposed Findings 154

Proposed Finding 154 states:

154. The Department's suggestion that the pension expense may be larger than necessary because the Company may not have reasonably managed its assets lacks proof in the record. The Department's claim is not based on any empirical evidence such as a comparison of the performance of the Company's pension assets to the performance of other pension funds of a comparable size. Nor has the Department demonstrated that a reasonable pension fund manager would have managed the assets differently. Rather, the Department has only expressed a general concern about the performance of the assets. This vague concern does not demonstrate that the Company's test year qualified pension expense is unreasonable and should be reduced as recommended by the Department.

The Department disagrees with the above proposed finding since the lack of pension asset recovery over the recent years of material robust economic recovery is extraordinary. Certainly, if Xcel's pension fund reflected market gains then it is unlikely that the Company would be seeking such significant sums from ratepayers for the 2008 market loss from over six years ago, and there should be material offsetting financial market gains based on recent financial market performance.

That said, the Department's principal concern is that no party other than Xcel bears a burden of proof in this matter. The Minnesota Supreme Court in *In re NSP*,⁶³ affirmed that point, as noted previously in these Exceptions. Given that one could read the above-quoted language to suggest that the Department bears a burden of proof as to why Xcel's pension fund has not shared in the market recovery, the Department recommends that this proposed finding be deleted. If the Commission wishes to adopt the Report's ultimate conclusions as to the 2008 market loss, this proposed finding is not needed for the Commission to do so.

For these reasons, the Department requests that Proposed Finding 154 be deleted as follows:

~~154.—The Department's suggestion that the pension expense may be larger than necessary because the Company may not have reasonably managed its assets lacks proof in the record. The Department's claim is not based on any empirical evidence such as a comparison of the performance of the Company's pension assets to the performance of other pension funds of a comparable size. Nor has the Department demonstrated that a reasonable pension fund manager would have managed the assets differently. Rather, the Department has only expressed a general concern about the performance of the assets. This vague concern does not demonstrate that the Company's test year qualified pension expense is unreasonable and should be reduced as recommended by the Department.~~

4. Exception to Proposed Findings 155-156

Proposed Findings 155 and 156 state, as follows:

155. Similarly, there is no evidence in the record to support the contention that the Company's pension expense should be reduced because the Company's retirement benefits are "generous" as claimed by the Department. To the contrary, the record shows that the Company's benefits are comparable to those of its peers, and its benefits for its new employees are lower than many of its peers. In addition, providing a competitive level of benefits is necessary for the Company to attract and retain the skilled employees who are needed to provide reliable service to ratepayers. [footnotes omitted]

⁶³ *In re NSP*, *supra*, 416 N.W.2d at 723, 725-26.

156. Likewise, the Department is mistaken when it claims that the Company is seeking "to get recovery of all of the 2008 market loss from ratepayers in the short term." As the Company explained, the Company is not seeking to recover all of the 2008 Market Loss in the short term. Rather, under FAS 87 and ACM, the loss is both phased-in and amortized resulting in recovery over the long-term. [footnotes omitted]

As to Proposed Finding 155, the Department did not and does not recommend a reduction in Xcel's pension benefit to its employees. As Ms. Campbell testified, the terms of employee benefits are negotiated matters of contract between Xcel and its employees.⁶⁴ The issue that Ms. Campbell addresses is the degree to which the 2008 market loss should be imposed on ratepayers in addition to ratepayers' already generous (100 percent) payment of qualified pension benefits (requiring no contribution to pension plans by the Company's employees) as well as paying for the "Company's" match of four percent regarding the voluntary 401K plan.⁶⁵ The Commission does not select the benefits offered by utilities, but it does determine the extent to which rates should reflect the costs of such benefits.

As to Proposed Finding 156, the Department noted that Xcel is not allowing its pension asset to recover in value (or not including financial market gains that should have occurred) before seeking from ratepayers (in this case and the 2012 rate case) very significant sums from ratepayers. This is what the Department meant by seeking recovery from ratepayers in the short term – it means no offset of the financial market returning to above 2007 market levels which clearly should have resulted in offsetting financial market gains.⁶⁶ For these reasons, the Department requests that Proposed Findings 155-156 be deleted, as follows:

⁶⁴ Ex. 429 at 103 (Campbell Direct).

⁶⁵ Ex. 435 at 90-91 (Campbell Surrebuttal); Ex. 450 at 6-7 (Campbell Opening).

⁶⁶ See Ex. 435 at 91 (Campbell Surrebuttal); Ex. 450 at 7 (Campbell Opening) (recommending that the 2008 market loss occurred but taking a longer period to recover the funds by allowing the pension funds to recover).

~~155. — Similarly, there is no evidence in the record to support the contention that the Company's pension expense should be reduced because the Company's retirement benefits are "generous" as claimed by the Department. To the contrary, the record shows that the Company's benefits are comparable to those of its peers, and its benefits for its new employees are lower than many of its peers. In addition, providing a competitive level of benefits is necessary for the Company to attract and retain the skilled employees who are needed to provide reliable service to ratepayers. [citations omitted]~~

~~156. — Likewise, the Department is mistaken when it claims that the Company is seeking "to get recovery of all of the 2008 market loss from ratepayers in the short term. As the Company explained, the Company is not seeking to recover all of the 2008 Market Loss in the short term. Rather, under FAS 87 and ACM, the loss is both phased in and amortized resulting in recovery over the long term. [citations omitted]~~

5. Proposed Findings 157-158

Proposed Findings 157-158 state, as follows:

157. Finally, contrary to the Department's assertion, there is no benefit to the shareholders from this longstanding approach to calculating pension expense because the Company does not pay out the gains to shareholders. Instead, the gains help to reduce rate increases by limiting the future pension expense. [footnote omitted]

158. For these reasons, the Administrative Law Judge concludes that the Company's approach of recognizing pension gains and losses is reasonable, and the Company's proposed phase-in and amortization of the 2008 Market Loss should be included in the 2014 test year expense. It would not be reasonable to exclude the effects of the 2008 Market Loss when ratepayers have benefited substantially from past market gains. The Department's recommendation to reduce the amount included in the test year expense related to the 2008 Market Loss is not supported by the record.

Xcel has confused the record to suggest erroneously that shareholders do not benefit from ratepayers paying 100 percent of the 2008 market loss or from not seeking to decrease rates when pension expense is negative. The Company has vigorously argued for ratepayer, not shareholder, payment for the 2008 market loss even though Xcel did not show why its pension assets did not adequately recover from a market loss in 2008. Making ratepayers pick up all of this expense certainly would benefit shareholders.

Moreover, to the extent that the Company's pension plan is overfunded in the future, then the Company's shareholders would benefit from not having to make payments into the pension fund even though pension expense continues to be recovered from ratepayers in rates.⁶⁷

The Department agrees that prior to 2008, Xcel's pension asset value reflected market gains; in this rate case, the Company has not shown why it is reasonable that its pension asset in this test-year does not reflect the very significant market gains that have occurred as of 2014. Thus, Xcel has not shown that it is reasonable for ratepayers to pay 100 percent of the 2008 market loss in this 2014 rate case.

For these reasons, Proposed Findings should be changed, as follows:

~~157. Finally, contrary to the Department's assertion, there is no benefit to the shareholders from this longstanding approach to calculating pension expense because the Company does not pay out the gains to shareholders. Instead, the gains help to reduce rate increases by limiting the future pension expense. [citation-omitted]~~

158. For these reasons, the ~~Commission Administrative Law Judge~~ concludes that the Company's approach of recognizing pension gains and losses is reasonable, and the Company's proposed phase-in and amortization of the 2008 Market Loss should not fully be included in the 2014 test year expense. ~~It would not be reasonable to exclude the effects of the 2008 Market Loss when ratepayers have benefited substantially from past market gains. The Department's recommendation to reduce the amount included in the test year expense related to the 2008 Market Loss by 50 percent is not supported by the record. [footnote: 450 at 6 (Campbell Opening).]~~

6. The Department continues to support its alternative recommendation if the Commission does not adopt Ms. Campbell's primary recommendations

Ms. Campbell summarized the Department's alternative recommendation in the event that the Commission chose not to accept her primary recommendations, as follows:⁶⁸

⁶⁷ See Ex. 435 at 89-95 (Campbell Surrebuttal); Ex. 450 at 7 (Campbell Opening).

⁶⁸ Ex. 450 at 7-8 (Campbell Opening).

Alternatively, if the Commission does not agree with my recommendations, then I would support the Company's second alternative normalization proposal modified as follows.

First, I do not agree that Xcel should be allowed to place any under-funded amount in rate base and earn a return on that amount, since the Company already receives a return on its prepaid pension asset (as discussed on pages 126-127 of Mr. Moeller's Direct Testimony, now adopted by Mr. Schrubbe). Allowing Xcel to earn a return on under-funding pension assets would give the Company an inappropriate incentive to make poor investment choices for pension assets. Instead, consistent with the Commission's determination in Xcel's prior rate case, I recommend that Xcel earn no return on any deferrals.

Second, I recommend that the overall normalization proposal from the last rate case should only impact Xcel's new alternative normalization proposals one and two, such that the \$1,054,357 deferral for 2013 XES cap that the Commission decided in Xcel's 2012 rate case should be allowed continued deferral.

Third, I recommend that Xcel only be allowed to defer this amount and be required to make a convincing case for why the Company should be allowed to amortize any unfunded balances in the future. For example, any future recovery by Xcel should be allowed only if Xcel can show that the Company made reasonable investment decisions regarding its pension assets.

Fourth, I recommend that Xcel's calculations of the allowed pension expense in each year be based on setting the discount rate equal to the EROA, which for example in 2014 would reduce pension costs by \$1.7 million and reduce Xcel's proposed \$18.246 million to \$16.5 million. DOC Ex. 435 at 101-102 (Campbell Surrebuttal).

The Department continues to support this alternative recommendation, as noted above.

CONCLUSION

For the reasons stated above, and consistent with its testimony and post-trial briefs in this matter, the Department respectfully requests that the Commission adopt the ALJ Report with the Limited Exceptions included herein.

Dated: January 20, 2015

Respectfully submitted,

/s/ **Julia E. Anderson**

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Docket No. E002/GR-13-868
Exhibit___(LHP-2), Schedule 2
Page 1 of 6Plant Rate Base Comparison
2015 over 2014
(\$ in 000s)**With Theoretical TD&G**

	2014 Average	2015 Average	2015 Step
Plant	16,132,459	17,378,470	643,745
Depreciation Reserve	7,563,040	7,989,715	17,180
ADIT	2,221,227	2,327,170	46,701
Rate Base	6,348,192	7,061,585	579,864
	2015 over 2014	713,393	
	Less 2015 Step	<u>(579,864)</u>	
Remaining Increase to Rate Base		133,529	
	2014 Historical Plant (2015 over 2014)	<u>(216,853)</u>	
Increase to Rate Base for 2015 Additions		<u><u>350,382</u></u>	

(\$ in 000s)

	Plant	Depreciation Reserve	ADIT
2014			
Per AEH Schedule 4 Page 2	16,132,459	7,563,040	1,965,989
Remove NOL			(255,238)
Per LHP Rebuttal Schedule	16,132,459	7,563,040	2,221,227 B
2015 Full			
Per AEH Schedule 27 Page 2	17,378,470	7,989,715	2,074,091
Remove NOL			(253,079)
Per LHP Rebuttal Schedule	17,378,470	7,989,715	2,327,170
2015 Step			
Per AEH Schedule 26 Page 2	16,776,204	7,488,786	2,055,296
Adjust Theoretical Reserve to 2015 Levels		(91,434)	36,382
Remove NOL			(249,014)
Per LHP Rebuttal Schedule	16,776,204	7,580,220	2,267,928 A
Change due to Step (A less B)	643,745	17,180	46,701

Xcel Energy
 Annual Revenue Requirement
 Passage of Time Reserve
 2014 Test Year Minnesota Electric Rate Case
 (000's)

Rate Analysis	Total Company	MN Jurisdiction
Plant Investment	225,127	138,460
Depreciation Reserve	369,867	269,895
CWIP		
Accumulated Deferred Taxes	29,385	19,821
	(174,125)	(150,755)
Average Rate Base	(174,125)	(150,755)
Debt Return	(3,970)	(3,437)
Equity Return	(9,002)	(7,794)
Current Income Tax Requirement	4,504	2,164
Book Depreciation	26,246	18,479
Annual Deferred Tax	(10,731)	(7,555)
ITC Flow Thru		
Tax Depreciation & Removal Expense		
AFUDC Expenditure		
Avoided Tax Interest		
Property Taxes		
Total Revenue Requirements	7,047	1,856

Capital Structure	Rate	Ratio	Weighted Cost
Long Term Debt	5.0200%	45.3000%	2.2700%
Short Term Debt	0.6800%	2.1400%	0.0100%
Preferred Stock	0.0000%	0.0000%	0.0000%
Common Equity	9.8300%	52.5600%	5.1700%
Required Rate of Return			7.4500%
PT Rate		0.0000%	
Composite Tax Rate	40.8870%		
MN Jur Demand after IA		74.3399%	

Plant Balance

Functional Class	2014 Avg Test Year	2014 Avg TCR	2014 Avg STEP	2014 Avg Test Year W/O STEP	2014 Allocator	2014 Avg Test Year W/O STEP MN JUR
Electric Intangible Plant	213,443,976			213,443,976	74.32%	158,633,585
Electric Steam Production Plant	2,334,671,336		24,816,179	2,309,855,157	74.34%	1,717,143,284
Electric Nuclear Production Plant	3,160,979,188		97,362,974	3,063,616,213	74.34%	2,277,488,261
Electric Hydro Production Plant	24,125,237			24,125,237	74.34%	17,934,670
Electric Other Production Plant	1,861,112,995			1,861,112,995	74.30%	1,382,725,441
Electric Transmission Plant	2,553,528,933	321,097,540	86,975,115	2,145,456,278	74.34%	1,594,929,373
Electric Distribution Plant	3,042,398,271		52,286,324	2,990,111,947	100.00%	2,990,111,947
Electric General Plant	359,372,942			359,372,942	74.29%	266,992,627
Common Intangible Plant	298,882,514			298,882,514	73.54%	219,785,369
Common General Plant	290,494,296			290,494,296	81.12%	235,645,321
Average Plant Balance	14,139,009,688		261,440,592	13,556,471,556		10,861,389,877

Functional Class	2015 Avg Test Year	2015 Avg TCR	2015 Avg STEP	2015 Avg Test Year W/O STEP	2015 Allocator	2015 Avg Test Year W/O STEP MN JUR
Electric Intangible Plant	226,185,085			226,185,085	73.99%	167,354,814
Electric Steam Production Plant	2,361,208,636		41,534,590	2,319,674,047	74.00%	1,716,486,548
Electric Nuclear Production Plant	3,281,131,819		158,913,389	3,122,218,430	74.00%	2,310,344,397
Electric Hydro Production Plant	24,333,077			24,333,077	74.00%	18,005,719
Electric Other Production Plant	1,865,679,258			1,865,679,258	73.95%	1,379,719,014
Electric Transmission Plant	2,804,453,954	451,082,423	143,806,419	2,209,565,112	74.00%	1,635,009,366
Electric Distribution Plant	3,083,738,304		71,174,100	3,012,564,204	100.00%	3,012,564,204
Electric General Plant	378,786,411			378,786,411	73.98%	280,228,862
Common Intangible Plant	320,327,566			320,327,566	73.46%	235,309,002
Common General Plant	302,265,799			302,265,799	81.00%	244,828,430
Average Plant Balance	14,648,109,909		415,428,498	13,781,598,989		10,999,850,357

Functional Class	2015 Avg over 2014 Avg Test Year W/O STEP Total Co.	2015 Avg over 2014 Avg Test Year W/O STEP MN JUR
Electric Intangible Plant	12,741,108	8,721,228
Electric Steam Production Plant	9,818,890	(656,735)
Electric Nuclear Production Plant	58,602,217	32,856,136
Electric Hydro Production Plant	207,840	71,050
Electric Other Production Plant	4,566,263	(3,006,427)
Electric Transmission Plant	64,108,834	40,079,993
Electric Distribution Plant	22,452,257	22,452,257
Electric General Plant	19,413,469	13,236,235
Common Intangible Plant	21,445,052	15,523,634
Common General Plant	11,771,503	9,183,109
Average Plant Balance	225,127,433	138,460,479

Accumulated Depreciation
 (DOC Information Request No. 2113 Modified to Include Total Company Rate Base and Annual Depreciation)

Functional Class	2014 Avg	2014 Avg	2014 Avg	2014	2014 Avg	Depr Expense	
	Test Year	STEP	Test Year W/O STEP	Allocator	Test Year W/O STEP MN JUR	Total Co.	MN JUR
Electric Intangible Plant	67,144,305	-	67,144,305	74.32%	49,902,284	16,779,431	12,470,632
Electric Steam Production Plant	1,379,954,744	1,053,363	1,378,901,381	74.34%	1,025,073,471	80,866,949	60,116,383
Electric Nuclear Production Plant	1,397,631,271	1,473,286	1,396,157,985	74.34%	1,037,902,008	99,205,015	73,748,878
Electric Hydro Production Plant	8,804,698	-	8,804,698	74.34%	6,545,401	1,229,445	913,968
Electric Other Production Plant	467,320,779	-	467,320,779	74.30%	347,198,871	65,132,612	48,390,678
Electric Transmission Plant	716,517,201	784,881	715,752,320	74.34%	532,089,333	49,909,746	37,102,840
Electric Distribution Plant	1,216,651,037	731,920	1,215,919,117	100.00%	1,215,919,117	69,370,448	69,370,448
Electric General Plant	141,925,927	-	141,925,927	74.29%	105,442,485	25,138,785	18,676,616
Common Intangible Plant	224,579,714	-	224,579,714	73.54%	165,146,280	28,156,407	20,705,013
Common General Plant	95,952,170	-	95,952,170	81.12%	77,835,193	22,297,494	18,087,447
Average Reserve Balance	5,716,481,844	4,023,450	5,712,458,394		4,563,054,442	458,086,333	359,582,902

Functional Class	2015 Avg	2015 Avg	2015 Avg	2015	2015 Avg	Total Co.	MN JUR
	Test Year	STEP	Test Year W/O STEP	Allocator	Test Year W/O STEP MN JUR		
Electric Intangible Plant	85,808,417	-	85,808,417	73.99%	63,489,826	20,564,458	15,215,685
Electric Steam Production Plant	1,455,597,576	2,106,726	1,453,490,850	74.00%	1,075,537,960	84,337,901	62,407,420
Electric Nuclear Production Plant	1,458,415,092	2,946,572	1,455,468,520	74.00%	1,077,001,374	106,844,779	79,061,809
Electric Hydro Production Plant	9,931,852	-	9,931,852	74.00%	7,349,261	1,104,863	817,564
Electric Other Production Plant	533,605,925	-	533,605,925	73.95%	394,615,654	65,465,697	48,413,609
Electric Transmission Plant	753,587,841	1,529,762	752,058,079	74.00%	556,499,556	50,746,982	37,551,186
Electric Distribution Plant	1,251,687,948	1,463,840	1,250,224,108	100.00%	1,250,224,108	70,151,610	70,151,610
Electric General Plant	169,078,830	-	169,078,830	73.98%	125,085,713	29,709,578	21,979,355
Common Intangible Plant	254,669,633	-	254,669,633	73.46%	187,077,428	32,029,020	23,528,156
Common General Plant	117,989,611	-	117,989,611	81.00%	95,568,904	23,377,244	18,935,036
Average Reserve Balance	6,090,372,726	8,046,900	6,082,325,826		4,832,449,785	484,332,131	378,061,430

Functional Class	2015 Avg over 2014 Avg		2015 Avg over 2014 Avg		Total Co.	MN JUR
	Test Year W/O STEP	Total Co.	Test Year W/O STEP	MN JUR		
Electric Intangible Plant		18,664,112		13,587,543		
Electric Steam Production Plant		74,589,469		50,464,489		
Electric Nuclear Production Plant		59,310,536		39,099,366		
Electric Hydro Production Plant		1,127,154		803,860		
Electric Other Production Plant		66,285,146		47,416,783		
Electric Transmission Plant		36,305,759		24,410,223		
Electric Distribution Plant		34,304,992		34,304,992		
Electric General Plant		27,152,904		19,643,228		
Common Intangible Plant		30,089,919		21,931,148		
Common General Plant		22,037,442		17,733,711		
Average Reserve Balance		369,867,432		269,395,343		
Average Deferred Balance		(153,014,157)		(111,448,853)		
Average Net Rate Base		(216,853,276)		(157,946,490)		
Debt Return				(3,601,180)		
Equity Return				(8,165,834)		
Current Tax Requirement				(5,761,906)		
Total Revenue Requirement				(17,528,919)		

Deferred Taxes

Functional Class	2014 Avg Test Year	2014 Avg TCR	2014 Avg STEP	2014 Avg Test Year W/O STEP	2014 Allocator	2014 Avg Test Year W/O STEP	MN JUR
Electric Intangible Plant	14,112,257		63,528	14,048,729	74.32%	10,441,149	
Electric Steam Production Plant	171,759,600		1,796,437	169,963,163	74.34%	126,350,392	
Electric Nuclear Production Plant	524,960,974		20,381,016	504,579,958	74.34%	375,104,077	
Electric Hydro Production Plant	2,219,357		-	2,219,357	74.34%	1,649,867	
Electric Other Production Plant	362,016,039		-	362,016,039	74.30%	268,962,061	
Electric Transmission Plant	431,781,785	40,370,905	9,346,035	382,084,846	74.34%	284,026,504	
Electric Distribution Plant	571,843,649		8,932,208	562,911,441	100.00%	562,911,441	
Electric General Plant	58,969,888		-	58,969,888	74.29%	43,811,104	
Common Intangible Plant	17,761,302		-	17,761,302	73.54%	13,060,899	
Common General Plant	25,452,528		-	25,452,528	81.12%	20,646,771	
Average Deferred Balance	2,180,877,379		40,519,224	2,099,987,251		1,706,964,263	

Functional Class	2015 Avg Test Year	2015 Avg TCR	2015 Avg STEP	2015 Avg Test Year W/O STEP	2015 Allocator	2015 Avg Test Year W/O STEP	MN JUR
Electric Intangible Plant	13,755,435		115,368	13,640,066	73.99%	10,092,313	
Electric Steam Production Plant	162,787,349		2,303,406	160,483,943	74.00%	118,753,119	
Electric Nuclear Production Plant	529,980,157		28,906,032	501,074,125	74.00%	370,779,247	
Electric Hydro Production Plant	2,083,783		-	2,083,783	74.00%	1,541,935	
Electric Other Production Plant	368,105,584		-	368,105,584	73.95%	272,223,787	
Electric Transmission Plant	480,730,828	53,890,094	15,186,311	411,654,422	74.00%	304,611,451	
Electric Distribution Plant	585,790,404		9,830,221	575,960,183	100.00%	575,960,183	
Electric General Plant	57,431,552		-	57,431,552	73.98%	42,488,268	
Common Intangible Plant	15,982,771		-	15,982,771	73.46%	11,740,762	
Common General Plant	22,955,921		-	22,955,921	81.00%	18,593,774	
Average Deferred Balance	2,239,603,782		56,341,338	2,129,372,349		1,726,784,839	

Functional Class	2015 Avg over 2014 Avg Test Year W/O STEP Total Co.	2015 Avg over 2014 Avg Test Year W/O STEP MN JUR
Electric Intangible Plant	(408,663)	(348,835)
Electric Steam Production Plant	(9,479,220)	(7,597,272)
Electric Nuclear Production Plant	(3,505,832)	(4,324,830)
Electric Hydro Production Plant	(135,574)	(107,933)
Electric Other Production Plant	6,089,545	3,261,726
Electric Transmission Plant	29,589,576	20,584,948
Electric Distribution Plant	13,048,742	13,048,742
Electric General Plant	(1,538,336)	(1,322,836)
Common Intangible Plant	(1,778,531)	(1,320,136)
Common General Plant	(2,496,608)	(2,052,997)
Average Deferred Balance	29,385,098	19,820,576