

DOCKET NO. 46936

APPLICATION OF SOUTHWESTERN	§	
PUBLIC SERVICE COMPANY FOR:	§	
A CERTIFICATE OF CONVENIENCE	§	
AND NECESSITY AUTHORIZING	§	PUBLIC UTILITY COMMISSION
CONSTRUCTION AND OPERATION	§	
OF WIND GENERATION AND	§	
ASSOCIATED FACILITIES IN HALE	§	
COUNTY, TEXAS AND ROOSEVELT	§	OF TEXAS
COUNTY, NEW MEXICO, AND	§	
RELATED RATEMAKING	§	
PRINCIPLES; AND APPROVAL OF A	§	
PURCHASED POWER AGREEMENT	§	
TO OBTAIN WIND GENERATED	§	
ENERGY	§	

DIRECT TESTIMONY

of

MARY P. SCHELL

on behalf of

SOUTHWESTERN PUBLIC SERVICE COMPANY

(Filename: SchellTXDirect.doc; Total Pages: 16)

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GLOSSARY OF ACRONYMS AND DEFINED TERMS

<u>Acronym/Defined Term</u>	<u>Meaning</u>
AFUDC	Allowance for Funds Used During Construction
NMPRC	New Mexico Public Regulation Commission
MW	Megawatt
SPS	Southwestern Public Service Company, a New Mexico corporation
SPS Wind Facilities	Wind generating facilities located in Hale County, Texas, and Roosevelt County, New Mexico
Xcel Energy	Xcel Energy Inc.

LIST OF ATTACHMENTS

<u>Attachment</u>	<u>Description</u>
MPS-1	IHS Global Insights Interest Rate Forecasts (<i>Non-native format</i>)
MPS-2	Page 33 from SPS's Form 10-K for the fiscal year ended December 31, 2016 (<i>Non-native format</i>)

**DIRECT TESTIMONY
OF
MARY P. SCHELL**

1 **I. WITNESS IDENTIFICATION AND QUALIFICATIONS**

2 **Q. Please state your name and business address.**

3 A. My name is Mary P. Schell. My business address is 414 Nicollet Mall, 401-4,
4 Minneapolis, Minnesota 55401.

5 **Q. On whose behalf are you testifying in this proceeding?**

6 A. I am filing testimony on behalf of Southwestern Public Service Company, a New
7 Mexico corporation (“SPS”) and wholly-owned electric utility subsidiary of Xcel
8 Energy Inc. (“Xcel Energy”).

9 **Q. By whom are you employed and in what position?**

10 A. I am the Director of Corporate Financial Policy for Xcel Energy and Assistant
11 Treasurer for SPS.

12 **Q. Please briefly outline your responsibilities as Director of Corporate Financial**
13 **Policy.**

14 A. I am responsible for providing leadership and technical expertise within the Treasury
15 department, which includes recommending and implementing the financing required
16 to achieve SPS’s target capital structure. In addition, I provide expertise regarding
17 financial analysis and develop financing and financial testimony on behalf of Xcel
18 Energy’s subsidiaries.

19 **Q. Please describe your educational background.**

20 A. I received my Bachelor of Science degree in Business in 1981 from Mankato State
21 University and my Master of Business Administration degree with a concentration in

1 Accounting in 1989 from the University of Minnesota, Carlson School of
2 Management.

3 **Q. Please describe your professional experience.**

4 A. I worked for The Pillsbury Company in Corporate Finance for eight years in
5 economic and financial analyses positions prior to my employment at Xcel Energy. I
6 have been employed in the Corporate Finance/Treasury department of Xcel Energy
7 and its predecessor companies since October 1991. I have had positions of
8 increasing responsibility since 1991, and I have been Director of Corporate Financial
9 Policy since 2000.

10 **Q. Have you previously provided testimony to any regulatory commission?**

11 A. Yes. I testified before the Public Utility Commission of Texas in Docket No. 43695
12 on financial integrity, cost of debt, and capital structure. I also submitted pre-filed
13 testimony on the same topics in two other SPS rate cases, Docket Nos. 45524 and
14 42004. In addition, I have testified before the Colorado Public Utilities Commission
15 and the Arizona Corporation Commission on capital structure and the cost of capital,
16 and I have submitted pre-filed testimony before the Public Service Commission of
17 Wisconsin and the North Dakota Public Service Commission on capital structure and
18 the cost of capital. I submitted prefiled testimony on financial integrity, cost of debt,
19 and capital structure in SPS's recent base rate cases before the New Mexico Public
20 Regulation Commission ("NMPRC"), including Case Nos. 16-00269-UT,
21 15-00139-UT, and 15-00296-UT, and I have testified before the NMPRC regarding
22 debt issuances on numerous occasions.

1 **II. ASSIGNMENT AND SUMMARY OF TESTIMONY**

2 **Q. What is your assignment in this proceeding?**

3 A. As explained in more detail by other SPS witnesses, SPS is planning to develop,
4 own, and operate two wind generating facilities: a 478 megawatt (“MW”) wind
5 generating facility located in Hale County, Texas, and a 522 MW wind generating
6 facility located in Roosevelt County, New Mexico (collectively, the “SPS Wind
7 Facilities”). SPS estimates that its total capital investment in the SPS Wind Facilities
8 will be approximately \$1.6 billion. My testimony explains how SPS plans to finance
9 the cost of the two facilities. SPS will also enter into a purchased power agreement
10 as part of the SPS Wind Facilities project. I will briefly discuss the general effect of
11 the purchased power agreement on SPS’s financial position.

12 **Q. Please summarize your testimony.**

13 A. SPS plans to finance the cost of the SPS Wind Facilities in a manner similar to
14 financing its other utility capital expenditures. SPS uses a combination of internal
15 funds, short-term borrowings, long-term debt, and equity to fund its capital
16 expenditure program. Because SPS intends to issue new debt and to obtain equity
17 from its parent company to pay for the cost of the SPS Wind Facilities, the financing
18 of these facilities will not have a material adverse effect on SPS’s financial integrity,
19 assuming SPS gets timely cost recovery.

20 **Q. Are Attachments MPS-1 and MPS-2 true and correct copies of the documents**
21 **you represent them to be?**

22 A. Yes.

1 **III. FINANCING OF THE SPS WIND FACILITIES**

2 **Q. What sources of funding does SPS plan to use to finance the capital costs**
3 **associated with the SPS Wind Facilities?**

4 A. SPS plans to finance its investment in the SPS Wind Facilities in the same manner as
5 it finances any other utility capital expenditures: by using a combination of internal
6 funds, short-term debt, long-term debt and equity contributions from its parent, Xcel
7 Energy. Because SPS's internal funds are generally insufficient to cover its capital
8 expenditures, SPS will require financing from external sources and will first issue
9 short-term debt to finance part of the construction costs.

10 **Q. Does SPS plan to use its currently outstanding long-term debt issuances to pay**
11 **for the costs of the SPS Wind Facilities?**

12 A. No. SPS plans to issue additional long-term debt to finance the cost of the SPS Wind
13 Facilities. As I will discuss in more detail below, Xcel Energy also plans to infuse
14 additional equity into SPS to maintain a target regulated capital structure composed
15 of 53.97% equity and 46.03% long-term debt.

16 **Q. How much additional long-term debt does SPS intend to issue for purposes of**
17 **financing the SPS Wind Facilities?**

18 A. At this time, SPS does not plan to issue project financing specifically for the SPS
19 Wind Facilities. As SPS's outstanding short-term debt level increases with funding
20 requirements, SPS will issue long-term debt to repay outstanding short-term debt,
21 and will receive parental equity infusions to maintain the target capital structure.
22 From 2018 through 2020, SPS plans to issue over \$1 billion in long-term debt to
23 repay short-term debt initially issued to fund capital expenditures. During this

1 period, SPS will also have \$250 million in maturing long-term debt. Consistent with
2 the construction schedule of the SPS Wind Facilities and other capital expenditures,
3 SPS will likely undertake a series of bond issuances during the period 2018 through
4 2020.

5 **Q. Have you estimated a long-term debt rate for the incremental debt that SPS**
6 **plans to incur for construction of the SPS Wind Facilities?**

7 A. Yes. SPS uses IHS Global Insight, an econometric forecasting service, as a source of
8 forecasted U.S. Treasury rates. The February 2017 Global Insight report forecasts
9 30-year Treasury rates ranging from 3.62% to 4.57% during the period from 2018
10 through 2020.¹ Because SPS's debt is riskier than U.S. Treasury debt, a credit spread
11 is added to the Treasury yield to derive an interest rate. Assuming no change in
12 credit ratings and based on the current forecast, SPS expects debt rates to range from
13 4% to 6% between now and 2020. SPS has used 4.25% as the cost of debt in
14 calculating the revenue requirement and the present value of the savings generated
15 by the SPS Wind Facilities. Those calculations are presented in the direct
16 testimonies of SPS witnesses Arthur P. Freitas and Jonathan S. Adelman,
17 respectively. The 4.25% is a reasonable interest cost assuming SPS issues a
18 combination of 10- and 30-year first mortgage bonds, has a capital structure that
19 includes 53.97% common equity, and maintains its current bond rating.

20 **Q. How much additional equity does Xcel Energy plan to invest in SPS to finance**
21 **the cost of the SPS Wind Facilities?**

22 A. Xcel Energy plans to infuse approximately \$1 billion of equity into SPS between

¹ See Attachment MPS-1

1 2018 and 2020. Because the purpose of infusing equity is to help SPS maintain its
2 target regulated capital structure, the equity infusions will likely occur on a schedule
3 that closely matches the debt issuances.

4 **Q. If SPS avails itself of the use of short-term debt during the construction phase,**
5 **from whom will it obtain the short-term loans?**

6 A. At this time, SPS does not plan to have a separate short-term facility/construction
7 revolver for the SPS Wind Facilities. Instead, SPS plans to issue commercial paper
8 to fund wind and other capital investments. Commercial paper is SPS's lowest cost
9 form of external financing. SPS has a \$400 million revolving credit agreement to
10 support its commercial paper program. SPS will re-evaluate its liquidity needs and
11 could consider upsizing its current credit agreement or evaluate other arrangements.

12 **Q. Have you estimated a short-term debt rate that SPS is likely to incur for the**
13 **amounts it borrows to construct the SPS Wind Facilities?**

14 A. Yes. Based on the IHS Global Insight forecast for short-term debt rates, SPS's
15 short-term debt interest costs will range from 2% to 4% from 2018 through 2020.²
16 These rates include a credit spread for SPS's credit rating.

17 **Q. What is the financial effect of the purchase and construction of the SPS Wind**
18 **Facilities on SPS?**

19 A. SPS had total net property, plant, and equipment of \$4.7 billion at December 31,
20 2016.³ The SPS Wind Facilities, which are estimated to cost approximately \$1.6
21 billion, will represent about 35% of SPS's net property, plant, and equipment. Thus,

² See Attachment MPS-1.

³ See Attachment MPS-2.

1 the SPS Wind Facilities represent a significant investment for SPS, but as discussed
2 by SPS witness David T. Hudson, those facilities will generate approximately \$2.8
3 billion in customer benefits over 25 years. SPS does not anticipate a major effect on
4 its financial position as a result of the investment in the SPS Wind Facilities,
5 provided that SPS receives timely recovery of the construction costs, including a cost
6 of capital that reflects a 53.97% equity ratio, and also receives timely recovery of the
7 ongoing operating costs of the SPS Wind Facilities. It is important for SPS to
8 maintain a strong capital structure during this period of large capital expenditures to
9 issue long-term debt at attractive rates. Mr. Hudson and SPS witness Evan D. Evans
10 discuss SPS's request for regulatory treatment prior to the SPS Wind Facilities being
11 included in base rates in more detail in their testimony. And as they note, timely and
12 adequate recovery of the costs of the SPS Wind Facilities is a major consideration in
13 SPS's investment decision.

14 **Q. What is the estimated dollar amount of Allowance for Funds Used During**
15 **Construction ("AFUDC") associated with the construction of the SPS Wind**
16 **Facilities?**

17 A. The estimated AFUDC associated with the SPS Wind Facilities is approximately \$55
18 million. This brings the total cost of the SPS Wind Facilities to approximately
19 \$1.655 billion.

20 **Q. What is the financial effect of SPS entering into a purchased power agreement**
21 **as part of this project?**

22 A. Purchased power agreements are considered to be debt-like in nature and are viewed
23 as fixed obligations. Although purchased power agreements are not itemized on the

1 balance sheet, the rating agencies include these obligations in the credit metric
2 analysis. This off-balance-sheet obligation further necessitates that SPS maintain
3 and earn on a 53.97% equity ratio, consistent with the original cost estimate and
4 analysis of this project.

5 **Q. Does this conclude your pre-filed direct testimony?**

6 A. Yes.

AFFIDAVIT

STATE OF MINNESOTA)
)
COUNTY OF HENNEPIN)

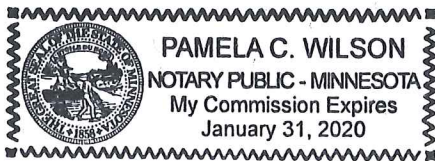
MARY P. SCHELL, first being sworn on her oath, states:


I am the witness identified in the preceding testimony. I have read the testimony and the accompanying attachments and am familiar with their contents. Based upon my personal knowledge, the facts stated in the testimony are true. In addition, in my judgment and based upon my professional experience, the opinions and conclusions stated in the testimony are true, valid, and accurate.



MARY P. SCHELL

Subscribed and sworn to before me this 9th day of March, 2017 by MARY P. SCHELL.





Notary Public, State of Minnesota
My Commission Expires: 1/31/2020

CERTIFICATE OF SERVICE

I certify that on March 21, 2017, this instrument was filed with the Public Utility Commission of Texas, and a true and correct copy of it was served by hand delivery on the Staff of the Public Utility Commission of Texas and the Office of Public Utility Counsel, and by hand delivery, next business day courier delivery, or first class mail on each party of record in SPS's most recent base rate case, Docket No. 45524.





Created on Tue 7 Feb 2017, 12:04 PM EST (17:04 GMT)

Frequency	Last Update	Short Label	End Date	Unit	Start Date	Source	SeriesType	2018.01	2018.02	2018.03	2018.04	2019.01	2019.02	2019.03	2019.04	2020.01	2020.02	2020.03	2020.04
QUARTERLY	2/6/2017	Rate on 90-day prime commercial paper Source	2027.04	% per annum	1971.02	IHS Economics	U.S. Macro - 10 Year Baseline	1.77	1.86	2.10	2.35	2.59	2.84	3.09	3.25	3.25	3.25	3.25	3.25
QUARTERLY	2/6/2017	Rate on Aa-rated public utility bonds Source	2027.04	% per annum	1959.01	IHS Economics	U.S. Macro - 10 Year Baseline	4.81	5.10	5.31	5.47	5.59	5.70	5.79	5.97	6.03	6.03	6.03	6.03
QUARTERLY	2/6/2017	Rate on 3-month eurodollar deposits Source	2027.04	% per annum	1977.01	IHS Economics	U.S. Macro - 10 Year Baseline	1.90	1.98	2.23	2.49	2.74	3.00	3.25	3.42	3.42	3.42	3.42	3.42
QUARTERLY	2/6/2017	Prime rate at commercial banks Source	2027.04	% per annum	1959.01	IHS Economics	U.S. Macro - 10 Year Baseline	4.50	4.54	4.79	5.04	5.29	5.54	5.79	6.00	6.00	6.00	6.00	6.00
QUARTERLY	2/6/2017	Yield on 10-year Treasury notes Source	2027.04	% per annum	1959.01	IHS Economics	U.S. Macro - 10 Year Baseline	2.94	3.04	3.24	3.38	3.54	3.74	4.00	4.07	4.07	4.07	4.07	4.07
QUARTERLY	2/6/2017	Yield on 30-year Treasury bonds Source	2027.04	% per annum	1977.02	IHS Economics	U.S. Macro - 10 Year Baseline	3.62	3.70	3.85	3.93	4.09	4.29	4.52	4.57	4.57	4.57	4.57	4.57
QUARTERLY	2/6/2017	Yield on 2-year Treasury notes Source	2027.04	% per annum	1976.03	IHS Economics	U.S. Macro - 10 Year Baseline	1.83	2.04	2.31	2.50	2.69	2.93	3.14	3.24	3.23	3.23	3.23	3.23
QUARTERLY	2/6/2017	Yield on 5-year Treasury notes Source	2027.04	% per annum	1959.01	IHS Economics	U.S. Macro - 10 Year Baseline	2.34	2.45	2.62	2.80	2.99	3.19	3.41	3.54	3.57	3.57	3.57	3.57
QUARTERLY	2/6/2017	Discount rate on 3-month Treasury bills Source	2027.04	% per annum	1959.01	IHS Economics	U.S. Macro - 10 Year Baseline	1.39	1.51	1.74	1.98	2.16	2.42	2.63	2.85	2.85	2.85	2.85	2.85
QUARTERLY	2/6/2017	Discount rate on 6-month Treasury bills Source	2027.04	% per annum	1959.01	IHS Economics	U.S. Macro - 10 Year Baseline	1.58	1.72	1.96	2.20	2.37	2.63	2.83	3.00	3.01	3.01	3.01	3.01
QUARTERLY	2/6/2017	Yield on 52-week Treasury bills or 1-year Treasury notes Source	2027.04	% per annum	1959.01	IHS Economics	U.S. Macro - 10 Year Baseline	1.74	1.93	2.17	2.41	2.60	2.86	3.06	3.21	3.21	3.21	3.21	3.21

Source: Global Insight, February 2017

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-K

(Mark One)

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2016

or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission file number: 001-03789

SOUTHWESTERN PUBLIC SERVICE COMPANY

(Exact name of registrant as specified in its charter)

New Mexico

75-0575400

State or other jurisdiction of incorporation or organization

(I.R.S. Employer Identification No.)

Tyler at Sixth, Amarillo, Texas 79101

(Address of principal executive offices)

Registrant's telephone number, including area code: **303-571-7511**

Securities registered pursuant to Section 12(b) of the Act: **None**

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. ☐ Yes ☒ No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. ☐ Yes ☒ No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ☒ Yes ☐ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 and Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ☒ Yes ☐ No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulations S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☒

Smaller Reporting Company ☐

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). ☐ Yes ☒ No

As of Feb. 24, 2017, 100 shares of common stock, par value \$1 per share, were outstanding, all of which were held by Xcel Energy Inc., a Minnesota corporation.

DOCUMENTS INCORPORATED BY REFERENCE

The information required by Item 14 of Form 10-K is set forth under the heading "Independent Registered Public Accounting Firm – Audit and Non-Audit Fees" in Xcel Energy Inc.'s definitive Proxy Statement for the 2017 Annual Meeting of Stockholders which definitive Proxy Statement is expected to be filed with the SEC on or about April 4, 2017. Such information set forth under such heading is incorporated herein by this reference hereto.

Southwestern Public Service Company meets the conditions set forth in General Instruction I(1)(a) and (b) of Form 10-K and is therefore filing this form with the reduced disclosure format permitted by General Instruction I(2).

SOUTHWESTERN PUBLIC SERVICE CO.
BALANCE SHEETS
(amounts in thousands, except share and per share data)

	Dec. 31	
	2016	2015
Assets		
Current assets		
Cash and cash equivalents	\$ 844	\$ 834
Accounts receivable, net	74,190	71,166
Accounts receivable from affiliates	949	1,079
Accrued unbilled revenues	119,418	103,781
Inventories	38,505	37,546
Regulatory assets	38,721	31,541
Derivative instruments	5,114	12,952
Prepaid taxes	21,779	35,666
Prepayments and other	7,855	20,520
Total current assets	307,375	315,085
Property, plant and equipment, net	4,695,819	4,348,823
Other assets		
Regulatory assets	346,683	301,814
Derivative instruments	22,113	25,272
Other	7,477	3,449
Total other assets	376,273	330,535
Total assets	\$ 5,379,467	\$ 4,994,443
Liabilities and Equity		
Current liabilities		
Current portion of long-term debt	\$ —	\$ 200,000
Short-term debt	50,000	15,000
Accounts payable	176,157	146,794
Accounts payable to affiliates	14,414	29,135
Regulatory liabilities	41,577	98,305
Taxes accrued	39,742	33,374
Accrued interest	19,162	17,781
Dividends payable	30,870	12,538
Derivative instruments	3,565	3,565
Other	29,703	35,654
Total current liabilities	405,190	592,146
Deferred credits and other liabilities		
Deferred income taxes	989,137	860,744
Regulatory liabilities	233,454	229,584
Asset retirement obligations	28,663	27,233
Derivative instruments	23,513	27,078
Pension and employee benefit obligations	107,872	93,346
Other	24,084	17,841
Total deferred credits and other liabilities	1,406,723	1,255,826
Commitments and contingencies		
Capitalization		
Long-term debt	1,635,858	1,338,522
Common stock — 200 shares authorized of \$1.00 par value; 100 shares outstanding at Dec. 31, 2016 and 2015, respectively	—	—
Additional paid in capital	1,446,223	1,371,223
Retained earnings	486,763	438,007
Accumulated other comprehensive loss	(1,290)	(1,281)
Total common stockholder's equity	1,931,696	1,807,949
Total liabilities and equity	\$ 5,379,467	\$ 4,994,443

See Notes to Financial Statements