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BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

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RE: IN THE MATTER OF ADVICE LETTER NO. 1672-ELECTRIC FILED BY PUBLIC SERVICE COMPANY OF COLORADO TO REVISE ITS COLORADO PUC NO. 7-ELECTRIC TARIFF TO IMPLEMENT A GENERAL RATE SCHEDULE ADJUSTMENT AND OTHER RATE CHANGES EFFECTIVE JULY 18, 2014.	**)))))))))**	**PROCEEDING NO. 14AL-________E**

<u>DIRECT TESTIMONY AND ATTACHMENTS OF RUTH K. LOWENTHAL</u>

ON

BEHALF OF

PUBLIC SERVICE COMPANY OF COLORADO

June 17, 2014

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

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SUMMARY OF DIRECT TESTIMONY OF RUTH K. LOWENTHAL

Ms. Ruth K. Lowenthal is the Senior Director, Total Rewards for Xcel Energy Services Inc. (“XES”). In this position, Ms. Lowenthal has responsibility for Employee Benefits for Retirement and Health and Welfare, Compensation, Payroll, and Human Resources (“HR”) Operations.

In her Direct Testimony, Ms. Lowenthal supports the known and anticipated adjustments to the 2013 level of compensation and benefits occurring during 2014 and 2015 and included in the Public Service Company of Colorado’s (“Public Service” or “Company”) January 1, 2015 through December 31, 2015 Test Year (“Test Year”) cost of service, which is supported by Ms. Deborah Blair.

Ms. Lowenthal shows that the 2013 total cash compensation, including salaries and wages for non-bargaining and bargaining employees adjusted to include 3.0 percent increases known and anticipated in both 2014 and 2015, and annual incentive and recognition program expenses are necessary for Public Service to be able to attract, retain, and motivate the employees it requires to provide safe, reliable electric service to its customers. She discusses the external market data that was relied upon to determine the 3.0 percent merit and base salary wage increases known and anticipated for 2014 and 2015 that have been included in the Test Year. She also presents the Confidential Towers Watson Compensation Study demonstrating that the total cash compensation provided by the Company to its employees and included in the Test Year are market competitive and therefore enables it to compete for the skilled employees needed to provide electric utility service.

Ms. Lowenthal also shows that the health and welfare and retirement benefits offered by the Company, including both its Defined Benefit and Defined Contribution Plans are reasonable and appropriate and remain at or below the level of such benefits provided by other regulated and non-regulated utilities with which it competes for employees. Ms. Lowenthal presents the results of the Joint Pension Study commissioned for purposes of assessing the reasonableness of the new pension plan applicable to non-bargaining employees hired after January 1, 2012 and agreed to as part of the Settlement Agreement entered into in Proceeding No. 11AL-947E, the Company's last Phase 1 electric rate case.

Ms. Lowenthal recommends that the Colorado Public Utilities Commission ("Commission") approve the level of Operations & Maintenance ("O&M") for the Total Rewards Program, which includes the known and anticipated adjustments to salaries and wages she discusses in her testimony, as well as the adjusted level of health and welfare and retirement expenses she discusses which are discussed in greater detail by Company witness Mr. Richard Schrubbe as reasonable and necessary to support Public Service's ability to provide safe and reliable electric service to its customers, and therefore is reasonable for inclusion in the Company’s Test Year cost of service supported by Ms. Blair.

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

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DIRECT TESTIMONY AND ATTACHMENTS OF RUTH K. LOWENTHAL

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GLOSSARY OF ACRONYMS AND DEFINED TERMS

Acronym/Defined Term	Meaning
ADA	Americans with Disabilities Act
AIP	Annual Incentive Program
Commission	Colorado Public Utilities Commission
DSM	Demand-Side Management
EEI	Edison Electric Institute
EPS	Earnings Per Share
ERISA	Employee Retirement Income Security Act
FMLA	Family & Medical Leave Act
HDHP	High Deductible Health Plan
HIPAA	Health Insurance Portability and Accountability Act
HR	Human Resources
HSA	Health Savings Account
IBEW	International Brotherhood of Electrical Workers
KPIs	Key Performance Indicators
LTI	Long-Term Incentive
O&M	Operations & Maintenance
OSHA	Occupational Safety and Health Administration
PEP	Pension Equity Plan

Acronym/Defined Term	Meaning
Public Service, or Company	Public Service Company of Colorado
RAR	Retail Average Rate
SAIDI	System Average Interruption Duration Index
STEM	Science, Technology, Engineering, and Math
Test Year	January 1, 2015 through December 31, 2015
UOR	Unplanned Outage Rate
VOC	Voice of Customer
Xcel Energy	Xcel Energy Inc.
XES	Xcel Energy Services Inc.

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO**

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DIRECT TESTIMONY AND ATTACHMENTS OF RUTH K. LOWENTHAL

I. INTRODUCTION, QUALIFICATIONS, PURPOSE OF TESTIMONY, AND RECOMMENDATION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Ruth K. Lowenthal. My business address is 414 Nicollet Mall, Minneapolis, Minnesota 55401.

Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR POSITION?

A. I am employed by Xcel Energy Services Inc. ("XES"), as Senior Director, Total Rewards. XES is a wholly-owned subsidiary of Xcel Energy Inc. ("Xcel Energy"), and provides an array of support services to Public Service Company of Colorado ("Public Service" or the "Company") and the other utility operating company subsidiaries of Xcel Energy on a coordinated basis.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?

A. I am testifying on behalf of Public Service.

Q. PLEASE SUMMARIZE YOUR RESPONSIBILITIES AND QUALIFICATIONS.

A. As Senior Director, Total Rewards, my areas of responsibility include Employee Benefits for Retirement and Health and Welfare, Compensation, Payroll, and Human Resources ("HR") Operations. I provide leadership and have strategic responsibility for designing, developing, and implementing a Total Rewards Program that aligns with other employers with whom Public Service and XES compete for employees (referred to herein as the "market") and enhances Xcel Energy's ability to attract, motivate, and retain talent at all levels throughout the organization. In addition, I am responsible for ensuring that our HR programs and services are administered accurately, cost-effectively, and efficiently. A statement of my qualifications, duties, and responsibilities is included as Attachment A.

Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY IN THIS PROCEEDING?

A. There are four purposes of my testimony. First, I describe the compensation and benefit programs that Public Service provides to its employees, explain how they are comparable to what is provided by the market, and are necessary for Public Service to be able to attract, retain, and motivate the employees it requires to provide safe, reliable electric service to its customers. Second, I show that the 2013 total cash compensation, including salaries and wages for non-bargaining and bargaining employees adjusted to include 3.0 percent increases known and anticipated in both 2014 and 2015, and annual incentive and recognition program expenses are reasonable when compared to what will be offered by the market.

Third, I show that the health and welfare and retirement benefits offered by the Company, including both its Defined Benefit and Defined Contribution Plans are reasonable and appropriate and remain at or below the level of such benefits provided by the market. Finally, I support the known and anticipated adjustments to the 2013 level of compensation and benefits occurring during 2014 and 2015 and included in the Company's January 1, 2015 through December 31, 2015 ("Test Year") cost of service, which is supported by Company witness Ms. Deborah Blair.

Q. ARE YOU SPONSORING ANY ATTACHMENTS AS PART OF YOUR DIRECT TESTIMONY?

A. Yes. I am sponsoring Confidential Attachment No. RKL-1 and Attachment Nos. RKL-2 through RKL-3.

Q. WHAT RECOMMENDATIONS ARE YOU MAKING IN YOUR TESTIMONY?

A. I recommend that the Colorado Public Utilities Commission ("Commission") approve the level of Operations & Maintenance ("O&M") for the Total Rewards Program presented in my testimony as reasonable and necessary to support Public Service's ability to provide safe and reliable electric service to its customers, and therefore is reasonable for inclusion in the Company's Test Year cost of service supported by Ms. Blair.

II. GOALS AND OBJECTIVES OF XCEL ENERGY'S TOTAL REWARDS PROGRAM

Q. WHAT ARE THE GOALS AND OBJECTIVES OF XCEL ENERGY'S TOTAL REWARDS PROGRAM?

A. Public Service's customers rely upon us to provide reliable, safe electric service twenty-four hours a day, seven days a week, 365 days a year. However, the planning, maintenance, and operation of an electric utility is highly complex and technically demanding. To meet our customers' needs, Public Service relies upon the skilled employees necessary to provide safe, reliable electric service. The goal of the Total Rewards Program is to attract, engage, and retain the necessary employees through market-competitive compensation and benefits. Only by providing market-competitive levels of compensation and benefits can the Company effectively compete with the market to attract, engage, and retain qualified employees.

Q. ARE THE EMPLOYEES ON WHOM PUBLIC SERVICE RELIES UPON ITS OWN EMPLOYEES?

A. As other witnesses have noted and as I note briefly above, XES is Public Service's service company affiliate and as such provides an array of support services and coordinates certain activities at Public Service and the other utility subsidiaries of Xcel Energy. As a consequence, Public Service does have many of its own employees, but it also relies on employees of XES to conduct its various utility and business activities. When I refer to "Public Service's" or "Xcel Energy's" employees in this context, they may be XES employees or Public Service employees. The goals and policies I describe apply to both.

Q. WHEN YOU REFER TO THE “MARKET,” WITH WHOM DOES XCEL ENERGY COMPETE FOR EMPLOYEES?

A. Xcel Energy competes for employees within both the utility and the non-utility sectors. Utility-sector competition generally takes place for jobs specific to utility operations and the delivery of utility services, such as control center operators, engineers, plant operators, technicians, welders, and machinists. The Company also competes with other utilities for corporate employees such as regulatory accountants and load forecasters. In addition, Xcel Energy competes with non-utility employers for jobs that are not specific to utilities, such as finance and accounting analysts, marketing analysts, designers, information technology specialists, human resource generalists, and customer service representatives.

Q. DOES THE COMPANY EXPERIENCE COMPETITION IN RECRUITING AND RETAINING EMPLOYEES?

A. Yes. Prospective employees with the skills and training required for the utility industry are in high demand. Many of our skilled trade crafts, such as linemen, welders, mechanics, and plant operators, require strong Science, Technology, Engineering and Math (“STEM”) skills, and four years of apprenticeship training after hire. These are well-trained individuals that are in high demand by contracting firms, utilities, and other sectors of the energy industry. In addition, we continue to see an imbalance in the supply and demand of engineers across a broad spectrum of production industries. Thus, there is a limited pool of candidates for many jobs within the Company and the Company competes for these jobs on a national, regional, and local basis.

Q. PLEASE PROVIDE EXAMPLES OF THE COMPANY'S RECRUITING CHALLENGES.

A. One example relates to the ability to attract engineers. In addition to competing with other utilities, the Company competes with consulting firms, which generally offer significantly higher pay and benefits according to feedback we receive from candidates. Due to the highly technical nature of the engineering responsibilities, Public Service, the other Xcel Energy system companies, and XES must often hire engineers with a senior level of experience, which is difficult to accommodate in our pay range. Recently we searched for two engineer openings and found no candidates that were willing to accept pay in the range in which we offer—despite the fact that our compensation is competitive with the utility market. In light of circumstances such as these, it isn't uncommon for Xcel Energy to hire engineers at higher job levels and provide additional benefits, such as paid time off to mitigate the overall lower compensation the Company offers.

Xcel Energy has also experienced challenges finding Senior Technical Instructors for our Safety area, particularly those that have experience as substation journeymen, relay technicians, and substation engineers. These employees are difficult to hire either because we cannot match their salary expectations or because they accept offers from other utilities.

As another example in Colorado, the Company has difficulty attracting candidates for our Transmission Planning department. These positions require specific utility experience, which includes knowledge of power system computer simulation programs and the system programming languages associated with these programs. Due to a limited talent pool in the electric utility industry for these jobs, it is critical for the Company to offer a competitive Total Rewards package to secure employees in these specialized positions.

Q. IN ADDITION TO THE RECRUITING AND RETENTION CHALLENGES EXPERIENCED DUE TO OTHER EMPLOYMENT OPPORTUNITIES IN THE MARKET, WHAT OTHER WORKFORCE CHALLENGES IS XCEL ENERGY FACING?

A. In addition to the competition Xcel Energy faces for employees, we project that approximately 50 percent of Xcel Energy's current workforce will retire in the next 10 years.

Q. WHAT LEVELS OF ATTRITION HAS PUBLIC SERVICE EXPERIENCED IN RECENT YEARS?

A. As I discuss in the later sections of my testimony, although Xcel Energy undertakes extensive efforts to ensure it provides market-competitive cash compensation, Public Service continues to experience a high level of attrition.

Table 1
Attrition by Year

	2010	2011	2012	2013	2014 (Actual through April 30)	2014* (Projected)
Attrition	4.3%	6.4%	8.9%	5.1%	2.2%	6.6%

*Includes actual numbers through April 2014 and is trended through year end.

Q. WHAT DOES THE ATTRITION DATA AND RETIREMENT OUTLOOK MEAN REGARDING THE NECESSITY TO PROVIDE MARKET COMPETITIVE COMPENSATION?

A. Given the current environment in which attrition for the Company and competition for employees is steadily increasing, and at the same time 50 percent of our workforce will retire in the next 10 years, it is imperative that Xcel Energy continue to provide market competitive compensation to employees who, in turn, provide safe, reliable electric service to Public Service's customers. Stability among our employee base is particularly crucial in a complex and highly skilled industry such as providing electric service. Thus, the Commission, Public Service, and Public Service's customers should be aligned in making sure the Company's compensation goals are met.

III. REASONABLENESS OF TOTAL CASH COMPENSATION COSTS INCLUDED IN THE PROPOSED REVENUE REQUIREMENT

Q. WHAT DOES THE TERM TOTAL CASH COMPENSATION MEAN?

A. Total Cash Compensation has three components: (1) base salary, (2) annual incentive, and (3) recognition. As described below, when combined these components compensate employees at a level that is comparable to the market.

Q. HOW DOES XCEL ENERGY ENSURE THAT THE CASH COMPENSATION IT PROVIDES TO EMPLOYEES IS COMPETITIVE WITH THE MARKET?

A. Xcel Energy undertakes a comprehensive job evaluation process, using external market data obtained from independent third-party surveys, to ensure its non-bargaining employee compensation is comparable to the market. Xcel Energy matches skill sets of jobs within the Company to the external market data to identify the market-competitive compensation rate that other companies that compete with Xcel Energy for employees are paying. Data is considered from a variety of surveys, including both utility and non-utility companies. Many of Xcel Energy's positions, however, exist only in the utility industry, so non-utility industry data is not used for those positions. When reviewing these surveys, essential job duties are defined in a position description. The 50th percentile of the survey data (that is, the median) is then used to determine the appropriate salary range for a position. Once an appropriate salary range is determined, the components of the compensation are broken up between: (1) base salary; and (2) either AIP or recognition compensation. By approaching cash compensation in this manner, the Company is able to ensure our employee compensation is comparable to the market and, thus, those costs are set at a reasonable level.

A. Base Salary

1. NON-BARGAINING EMPLOYEE BASE SALARY INCREASES

Q. PLEASE DESCRIBE HOW BASE SALARY INCREASES MAY BE EARNED.

A. Consistent with the Company's pay-for-performance and market-competitive philosophy, managers are allowed to award merit increases based on employees' performance, position in the salary range (an indicator of market), and internal equity. Merit awards tend to be higher for employees who have high performance ratings and are at the low end of the salary range. On the other hand, average performers who are at the higher end of the salary range for their job classification may only receive a small merit award and a poor performer will receive no merit increase.

Q. ARE THE BASE SALARY INCREASES YOU DESCRIBE FOR NON-BARGAINING EMPLOYEES THE SAME THING AS COST OF LIVING INCREASES?

A. No. An employee must earn a base salary increase based upon performance, among other factors. This is opposed to cost of living increases in base salary, which are typically provided regardless of performance and across the board to all employees. Xcel Energy has not historically provided the latter. In that regard, the base salary increases that can be earned by Xcel Energy employees are typically referred to as "merit base salary increases."

Q. HOW DOES THE COMPANY DETERMINE THE ANNUAL BUDGET FOR MERIT BASE SALARY INCREASES?

A. For non-bargaining employees, the Company balances a number of factors to arrive at budgeted merit base salary increases. The factors include: review of external market surveys regarding base salary increases; comparison of potential or negotiated wage increases to our bargaining employees; economic conditions; and company performance.

Q. WHAT MERIT BASE SALARY INCREASES WERE GIVEN IN 2013 AND 2014 TO NON-BARGAINING EMPLOYEES?

A. For 2013 and 2014, non-bargaining employees received a 2.75 percent and 3.0 percent merit base salary increase, respectively.

Q. CAN YOU DEMONSTRATE THAT A 2.75 PERCENT MERIT BASE SALARY INCREASE WAS APPROPRIATE FOR 2013?

A. Yes. Surveys demonstrate that a 2.75 percent increase in base salary is actually lower than what the market provided in 2013. In particular, six[1] different survey sources reported that 2013 increases fell within the following ranges:

- 3.0% - 3.3% for all utilities on a national basis; and
- 2.8% - 3.0% for all companies on a national basis.

These independent surveys include a comprehensive representation of many companies, both in the utility and general industry. Thus, providing a 2.75 base

1 WorldatWork "2013-2014 Salary Budget Survey"; The Conference Board "2013-2014 Salary Increase Budget Survey Results; Towers Watson, "2013 General Industry Salary Budget Survey"; Culpepper, "Salary Budget & Compensation Planning Survey Results 2013-2014"' Mercer "2013/2014 US Compensation Planning Survey Report"; and Aon Hewitt "U.S. Salary Increase Survey 2013-2014".

salary increase was reasonable, if not slightly behind, when compared to the market in 2013.

Q. IS A 3.0 PERCENT MERIT INCREASE IN BASE SALARY FOR NON-BARGAINING EMPLOYEES COMPARABLE TO WHAT THE MARKET IS EXPECTED TO PROVIDE IN 2014?

A. Yes. The same six surveys noted above demonstrate that a 3.0 percent increase in base salary is comparable to what the market is expected to provide in 2014. Similar to what was actually provided in 2013, the six surveys project 2014 base salary increases to fall within the following ranges:

- 3.0% - 3.3% for all utilities on a national basis; and
- 3.0% for all companies on a national basis.

Thus, providing a 3.0 percent merit base salary increase for non-bargaining employees in 2014 is reasonable and necessary if Xcel Energy's compensation is to remain competitive with the market.

Q. WHAT MERIT BASE SALARY INCREASE IS BUDGETED FOR NON-BARGAINING EMPLOYEES FOR 2015?

A. For 2015, the Company has budgeted a 3.0 percent merit base salary increase for non-bargaining employees expected to take effect in March, 2015.

Q. ARE STUDIES AVAILABLE TO SHOW WHAT BASE SALARY INCREASES ARE EXPECTED TO BE PROVIDED BY EMPLOYERS IN 2015?

A. No.

Q. IF NO BASE SALARY INCREASE STUDIES ARE AVAILABLE FOR 2015, WHY DOES PUBLIC SERVICE BELIEVE 3.0 PERCENT IS REASONABLE FOR 2015?

A. Although surveys are not yet available to show what employers are expected to provide in 2015, existing survey data can be used to demonstrate the reasonableness of a 3.0 percent increase for those years. In particular, the existing survey data show: (1) 3.0 percent in 2015 falls within ranges of base salary increases provided by employers in the most recent years; and (2) an upward trend of base salary increases to a level above 3.0 percent, which supports Public Service including a 3.0 percent base salary increase for 2015.

Q. PLEASE EXPLAIN FURTHER HOW A 3.0 PERCENT BASE SALARY INCREASE IN 2015 IS COMPARABLE TO THE RANGE AND TREND OF BASE SALARY INCREASES GIVEN BY EMPLOYERS IN RECENT YEARS?

A. Using the same base salary increase surveys discussed above, the following ranges of base salary increases were given by all companies and all utilities on a national basis for 2010 – 2014:

Table 2

Year	Range for all utilities on a national basis	Range for all companies on a national basis
2010	2.4 – 3.2 %	2.5 – 2.9 %
2011	2.8 – 3.3 %	2.7 – 3.0 %
2012	2.9 – 3.4 %	2.7 – 3.0 %
2013	3.0 – 3.3 %	2.8 – 3.0 %
2014*	3.0 – 3.3 %	3.0 %

** Based on projected increases expected to be provided by employers.*

Table 2 demonstrates a range of base salary increases between 2.4 – 3.4 percent for all utilities and 2.5 – 3.0 percent for all companies on a national basis between 2010 and 2014, with an upward trend during that time to 3.3 percent in 2013 and 2014 for all utilities. Based on my experience, I believe this level of base salary increases will be sustained in 2015. Thus, an annual 3.0 percent base salary increase for 2015 is representative, if not slightly lower, of what the market will provide and is reasonable for the Test Year cost of service.

Q. IN ADDITION TO THE SURVEY DATA, ARE THERE OTHER REASONS WHY A 3.0 PERCENT MERIT BASE SALARY INCREASE IS REASONABLE FOR 2015?

A. Yes. For Test Year cost of service purposes, the Company assumed no increase in headcount. At the same time, as explained by Company witness Ms. Mary Schell, the Company plans to again spend approximately $4 billion in capital expenditures during the next five year period, 2014 to 2018. Therefore, an increased amount of work is being requested from the current number of employees, thus increasing the productivity from employees.

Q. HAS THE COMPANY INCLUDED MERIT BASE SALARY INCREASES FOR NON-BARGAINING EMPLOYEES AS A PART OF ITS TEST YEAR COST OF SERVICE?

A. Yes. As discussed by Ms. Alice Jackson and Ms. Deborah Blair, Public Service is proposing to set prospective rates based on our historic 2013 O&M costs, with limited adjustments for known and anticipated changes that the Company expects to occur during 2014 and 2015. The labor costs included in the Test Year cost of service include adjustments for the 3.0 percent merit base salary increases that: (1) have been provided to non-bargaining employees in 2014;

and (2) are anticipated in 2015. The adjustments reflect costs already incurred by the Company or that have been budgeted for merit base salary increases and thus are representative for rate-making purposes. Ms. Blair describes how the adjustments were calculated for Test Year cost of service purposes.

2. BASE SALARY INCREASES FOR BARGAINING EMPLOYEES

Q. HOW ARE BARGAINING EMPLOYEE WAGE INCREASES DETERMINED?

A. Bargaining employee hourly wage increases, or general wage increases, are based on the collective bargaining agreement with the International Brotherhood of Electrical Workers ("IBEW") Local Union No. 111, which includes bargaining unit employees assigned to the electric utility. Xcel Energy uses market survey information as part of the process to negotiate a market competitive general wage increase for bargaining employees.

Q. WHAT IS THE STATUS OF THE CURRENT COLLECTIVE BARGAINING AGREEMENT?

A. The last collective bargaining agreement expired on May 31, 2014. Under that agreement, the last base salary increase was awarded on May 27, 2013 at an amount of 2.75 percent.

Q. WHEN WILL THE NEXT COLLECTIVE BARGAINING AGREEMENT BE NEGOTIATED?

A. Public Service is currently in the process of negotiating a new collective bargaining agreement with IBEW Local Union No. 111. This process is expected to continue into the summer of 2014. If the agreement is finalized prior to the filing of its rebuttal case, the Company will update the Test Year cost of service to incorporate any changes to the current assumptions in the Test Year.

Q. HAS THE COMPANY INCLUDED BASE SALARY INCREASES FOR BARGAINING EMPLOYEES AS A PART OF ITS TEST YEAR COST OF SERVICE?

A. Yes, the Test Year cost of service includes base salary increases of 3.0 percent annually for bargaining employees in 2014 and 2015. Ms. Blair describes how the adjustments were calculated for Test Year cost of service purposes.

Q. WHY IS IT REASONABLE TO INCLUDE BASE SALARY INCREASES FOR BARGAINING EMPLOYEES IF NO CURRENT COLLECTIVE BARGAINING AGREEMENT PROVIDES BASE SALARY INCREASES IN 2014 OR 2015?

A. Although no current agreement provides for base salary increases for 2014 or 2015, historically these types of increases have been a part of the collective bargaining agreements. Table 3 below shows the base salary increases for bargaining employees in recent years under collective bargaining agreements.

Table 3
Recent base salary increases for Public Service bargaining employees

6/1/2008-5/31/2009	4.10%
6/1/2009-5/31/2010	2.00%
6/1/2010-5/31/2011	4.00%
6/1/2011-5/31/2012	4.00%
6/1/2012-5/31/2013	2.75%
6/1/2013-5/31/2014	2.75%

In fact, base salary increases have been a part of the every collective bargaining agreement Xcel Energy has had with IBEW Local Union No. 111. Thus, it is reasonable to assume that base salary increases will be included in the next effective agreement and be effective starting in 2014.

Q. WHY ARE 3.0 PERCENT BASE SALARY INCREASE PROJECTIONS USED FOR BARGAINING EMPLOYEES IN 2014 AND 2015 IN THE TEST YEAR COST OF SERVICE?

A. A 3.0 percent increase in base salary for bargaining employees falls well within the average of historic base salary increases provided under prior collective bargaining agreements.

B. Annual Incentive Program (AIP)

Q. YOU STATED THAT XCEL ENERGY'S COMPENSATION STRUCTURE INCLUDES INCENTIVE PROGRAMS IN ADDITION TO BASE SALARY. WHAT IS THE ROLE OF THE INCENTIVE PROGRAMS IN THE COMPENSATION STRUCTURE?

A. Employers can provide cash compensation to employees either solely through base salary or through a combination of base salary and incentive compensation. Xcel Energy's AIP reflects the latter approach. That is, rather than providing all of an employee's compensation as base salary ("fixed pay"), Xcel Energy provides a portion as incentive compensation ("at-risk pay"). This compensation is a part of the total cash compensation package provided to employees, and it is only through inclusion of the AIP that Xcel Energy's compensation levels are competitive with what is paid by the market.

Q. IS IT COMMON PRACTICE FOR LARGE COMPANIES SUCH AS UTILITIES TO USE ANNUAL INCENTIVE COMPENSATION AS PART OF THEIR COMPENSATION PACKAGES?

A. Yes. The use of incentive compensation by employers is a prevalent practice throughout the United States. In fact, performance-based award programs, in which a portion of compensation must be re-earned each year, remained very high in 2013, with 90 percent of employers using this type of program according to an Aon Hewitt survey of 1,147 U.S. companies.[2] According to the 2013 Towers Watson Compensation Study, 99 percent of utilities in the national sample maintain an annual incentive plan, and 100 percent of utilities in the revenue-based sample maintain an annual incentive plan.

Q. WHY DOES XCEL ENERGY INCLUDE INCENTIVE COMPENSATION AS PART OF ITS OVERALL COMPENSATION PLAN?

A. There are two fundamental tenets related to incentive compensation that are well recognized: (1) it promotes superior employee performance; and (2) it reduces labor costs. Thus, Xcel Energy incorporates incentive compensation to provide these benefits for customers.

Q. PLEASE EXPLAIN HOW INCENTIVE COMPENSATION PROMOTES SUPERIOR EMPLOYEE PERFORMANCE.

A. A well-designed incentive compensation plan provides incentives for employees to meet specific goals. For example, Xcel Energy's AIP focuses on objectives that benefit customers, including promoting customer satisfaction, reliability,

2 http://aon.mediaroom.com/2013-08-29-Aon-Hewitt-Survey-Shows-2014-Salary-Increases-to-Reach-Highest-Levels-Since-2008

safety, and environmental goals. An employee receives annual incentive compensation only if the employee demonstrates that the employee has met his or her annual objectives, which motivates employees to accomplish these goals, thereby helping Xcel Energy and Public Service achieve overall operational excellence.

In addition, an approach that includes incentive compensation, in contrast to a pure base salary approach, strengthens the link between pay and performance, because the performance must occur in order for the pay to be realized. Using base salaries alone allows for the pay to be realized regardless of whether annual performance objectives are met or not. Thus, sole reliance on base salary would significantly limit Xcel Energy's ability to motivate and reward its employees for delivering superior performance.

Q. HOW DOES INCENTIVE COMPENSATION PROVIDE COST SAVINGS FOR CUSTOMERS?

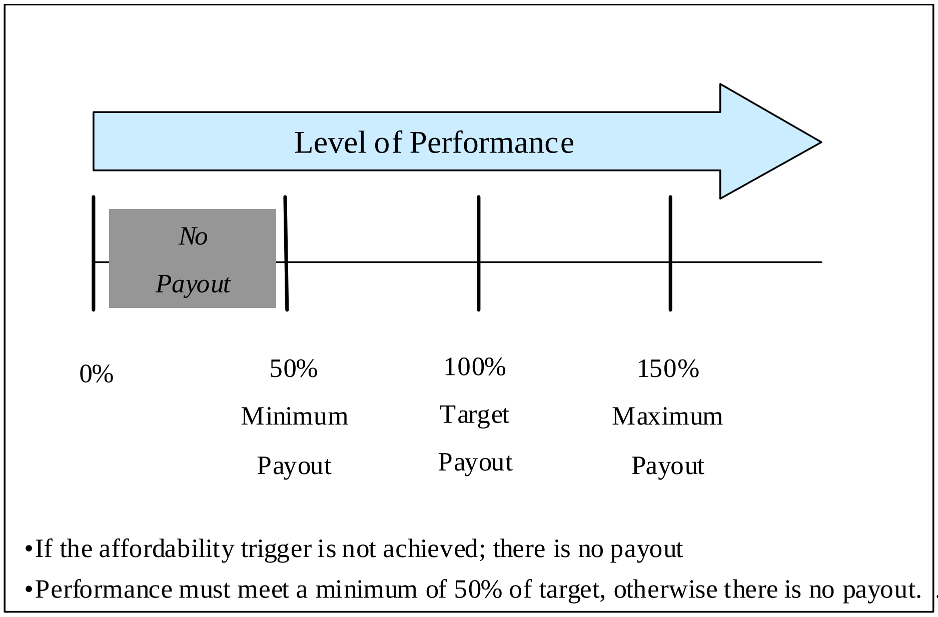
A. If Xcel Energy offered all compensation solely through base salary, a merit increase would become an annual fixed cost on the entire cash-based compensation. In contrast, the AIP requires the employee to re-earn the incentive reward every year, and if performance expectations are not met incentive pay is reduced or eliminated. Incentive pay, therefore, does not become a permanent fixed cost. Thus, by moving a portion of each employee's pay from base pay to incentive pay, the AIP reduces our overall labor costs by avoiding the compounding effect of annual base pay increases.

Q. PLEASE GENERALLY DESCRIBE HOW THE AIP IS STRUCTURED.

A. The AIP, which covers exempt, non-bargaining employees, uses metrics specifically focused on providing benefits to customers in the form of greater efficiencies in operations, increased customer satisfaction, improved reliability, environmental leadership, and higher safety levels. Each eligible employee has a targeted annual incentive expressed as a percentage of base salary. The percentage is determined by position/level within the organization, and, when combined with the employee's base salary, delivers a market-competitive level of total cash compensation. The program defines different levels of performance and allows employees to reach a percentage of their target award.

The target performance level assumes 100 percent achievement of individual, business area, and corporate performance components. Actual payments may exceed or fall below target for a given performance period based on performance. The program uses an overall funding governor -- the earnings per share ("EPS") of Xcel Energy -- as an affordability trigger for payments. If the overall affordability trigger for payment is not met, the program does not pay as it would not be prudent. The levels of performance and payout are illustrated in Figure 1 below:

Figure 1



Q. PLEASE DESCRIBE IN MORE DETAIL THE THREE PERFORMANCE COMPONENTS OF THE AIP.

A. The AIP includes the following components in Table 4:

Table 4

Performance Component	Types of Goals within Component	Purpose of Goals within Component
Individual	The individual component is based on the individual performance results of specific goals identified by the employee and his/her manager.	Goals are tied specifically to the employee's job functions and competencies and are developed in alignment with business area and corporate objectives.
Business Area	The business area component consists of goals and key performance indicators specific to the business area in which the employee works.	Goals are typically comprised of measures related to operational performance and are aligned to the corporate scorecard goals and priorities.
Corporate	The corporate component consists of goals and key performance indicators focused on operational, environmental and safety measures.	Goals represent customer and employee interests.

Q. ARE EACH OF THE THREE PLAN COMPONENTS EQUALLY IMPORTANT IN ASSESSING THE PERFORMANCE OF AN EMPLOYEE?

A. No. In assessing a particular employee's performance, the importance of each of the objectives will vary based upon the employee's position and level of responsibility. The weightings are designed such that the employee's goals are more strongly linked to objectives that he or she has the greatest potential to affect. For example, the weighting for non-supervisory employees focuses on the Individual and Business Area goals that are tied to customer satisfaction, safety, and reliability. In contrast, the weighting for more senior level positions focuses on Corporate goals. Table 5 shows the weightings of these different categories for the 2013 AIP.

Table 5

	2013 AIP Weights (Exempt, Non-Bargaining Employees)		
Salary Tiers/Grades	**Individual**	**Business Area**	**Corporate**
Exempt M, N, O* Engineer A, B*	75%	15%	10%
Exempt P, Q* Engineer C*	50%	30%	20%
Engineer D, E* Management R-T**	40%	30%	30%
Management U-V**	20%	30%	50%
Management W-X**	20%	30%	50%
Business Area Vice President	0%	40%	60%
Executives	0%	0%	100%

* Positions in these tiers are in operations or professional roles.

** Positions in these tiers are in professional, manager, director, or vice president roles.

Q. DO THE CATEGORY WEIGHTINGS CHANGE THE TOTAL AMOUNT OF TARGET INCENTIVE COMPENSATION THAT CAN BE EARNED?

A. No. The weightings modify the mix of accomplishments needed for employees to achieve the target levels, but do not change the target levels.

Q. HOW ARE THE GOALS IN EACH COMPONENT MEASURED?

A. For the individual component, employees have performance goals tied to their job functions. The business area and corporate components use key performance indicators ("KPIs"), which are designed to measure goals. Each business area uses a scorecard which contains several KPIs specific to that business function.

Q. HOW ARE SCORECARDS AND KPIs DESIGNED?

A. Scorecards and KPIs are designed to drive superior employee performance, which in turn delivers benefits to our customers. Goals are designed to be challenging, but achievable. When goals are met, the resulting incentive pay provides a total level of cash compensation that is market-competitive.

Q. HAS THE CORPORATE SCORECARD BEEN MODIFIED IN RECENT YEARS?

A. Starting with the 2012 AIP, "Earnings Results" was removed as a Corporate performance measure to more closely align goals to customer benefits. Thus, for the 2013 AIP plan, the Corporate scorecards do not rely upon Earnings Results. The 2013 Corporate scorecard is shown in Table 6 below:

Table 6

Goal	Key Performance Indicator (KPI)	Measurement
Operational Excellence	System Average Interruption Duration Index (SAIDI)	SAIDI measures the average annual duration of sustained interruptions seen by the average electric customer on our system.
	Unplanned Outage Rate (UOR)	UOR measures the percentage of time when a generating plant is not available for reasons other than planned outages.
Value to the Customer	Public Safety Index	The Public Safety Index measures response time to calls about our electric service from customers and contractors.
	Customer Value	The existing Voice of the Customer ("VOC") survey, which has been conducted since 2005, measures survey responses from residential, small business, and large business customers to the question: *Considering the price you pay relative to the quality of the products and services you receive, how would you rate Xcel Energy's overall value?*
Employee Safety and Engagement	OSHA Recordable Incident Rate	The OSHA Incident Rate is used to measure safety performance. OSHA Incident Rate is the standard measurement used in the utility and general industry.
	Employee Engagement	Our ability to utilize the full potential of our workforce requires that we foster a culture of engagement. Research shows that engaged employees are safer, more productive, commit more of their discretionary effort, and bring more positive energy to the communities we serve.
Environmental Leadership	Demand Side Management (GWh)	We measure actual results compared to goals presented in DSM programs filed and accepted by state regulators.

Q. HOW DO THE CORPORATE GOALS BENEFIT CUSTOMERS?

A. These corporate goals are designed to benefit all of our customers. The SAIDI and UOR KPIs benefit our customers because they focus on reliability of generation units and service to our customers. The SAIDI KPI focuses our employees on ensuring SAIDI is kept at a reasonable level. The UOR KPI is focused on reducing unplanned outages through improved work scheduling and planning, quality assurance, and human capital. The Company works to achieve a level of reliability that is consistent with the value our customers expect compared to the cost.

The Customer goal benefits customers because it measures whether we are meeting or exceeding our customers' expectations. The Customer Value KPI helps ensure that we are meeting our customers' expectations in other areas: it measures our customers' perception of customer service, service reliability, price, communications, company image, and billing. The Public Safety Index KPI measures our public safety performance. The Public Safety Index includes a variety of metrics, including contacts to our electric service lines; contractor communication to provide information concerning working safely where overhead lines are present; and training for electric first responders.

The Employee goal helps to ensure that we have a safe and productive workforce to deliver service to our customers. Safety is a core value of Xcel Energy: the OSHA Recordable Incident Rate KPI reinforces its importance. The higher the safety level of our employees, the more productive and reliable the service. Similarly, engaged employees are necessary to every facet of our business – especially in today's environment, as we seek to improve productivity and keep our costs competitive for our customers.

Finally, the Environmental Leadership goal tracks the results achieved by Public Service compared to the Demand Side Management ("DSM") goals established by state regulators. State regulators and legislators have created important public policies such as DSM. By adhering to such important public policies, employees' actions directly benefit customers.

Q. IS IT REASONABLE TO INCLUDE EPS AS AN AFFORDABILITY TRIGGER?

A. Yes. Payment of incentive compensation in the face of poor financial performance is not reasonable. The trigger is used to ensure payment of the AIP can be made, not to guarantee payments are made. Individuals must earn incentive pay through performance by achieving individual, business unit, and corporate goals. This serves to balance healthy financial performance and operational excellence to truly deliver maximum benefits to customers.

Q. HAS THE COMPANY TAKEN STEPS TO MITIGATE AIP COSTS?

A. Yes. Effective in 2011, non-exempt, non-bargaining employees who previously were included in the AIP at a 6 percent target payout percentage are no longer eligible for the AIP. To ensure that non-exempt employees nonetheless continue to be paid at market levels, their base wages were increased up to 3.0 percent.

In the last several years we have also made other cost-saving design changes to the program. The Company eliminated eligibility for employees hired on or after October 1 of a program year because they will not have been in the job long enough to produce results for that year. Another change is that incentive awards are prorated for employee job movement that results in a change in incentive opportunity. In other words, if an employee moves from a position with a 6 percent target to position with a 10 percent target, the award will be calculated based on the actual time the employee was in each job rather than the higher target for the entire year. The Company also added a provision that employees must be employed with Xcel Energy on the actual date the AIP is paid, meaning that employees who voluntarily leave the Company will not receive an award if they leave before the payment date. Finally, we eliminated all incentive pay (not just the amount linked to individual performance) for any employee who was not performing at a successful level.

Q. WHAT AMOUNT OF AIP COSTS DOES PUBLIC SERVICE SEEK TO RECOVER IN THIS CASE?

A. The Company requests recovery of $9,545,319 for AIP expense. This is the target amount of AIP expense incurred by the Company in 2013, but includes adjustments to account for merit base salary increases in 2014 and anticipated for 2015 for non-bargaining employees. I demonstrated the reasonableness of these merit base salary increases earlier in my testimony. Ms. Blair describes how the adjustments were calculated for Test Year cost of service purposes.

C. Recognition Programs

Q. PLEASE SUMMARIZE XCEL ENERGY'S RECOGNITION PROGRAMS.

A. The recognition programs are a years-of-contribution program, a corporate recognition program, and the Spot On Award program. The years-of-contribution program recognizes employee loyalty and cumulative career effort every five years. The corporate recognition program provides thank you cards, nominal gift cards, small gifts, or items with the Xcel Energy logo to recognize individuals and groups of employees for above-and-beyond performance. The Spot On Award program was created as a tool for managers to reward outstanding performance for non-exempt, non-bargaining employees (i.e., those removed from eligibility for the AIP in 2011).

Q. WHAT AMOUNT HAS THE COMPANY INCLUDED IN THE TEST YEAR COST OF SERVICE FOR RECOGNITION PROGRAMS?

A. For Test Year purposes, the Company has used the costs it actually incurred in 2013 for the recognition programs. In particular, the 2013 historical costs for the recognition programs were:

Table 7

Recognition Program	**2013 Historical Amounts**
Performance Recognition and Years of Contribution	$392,891
Spot On Award	$101,896
Total	$494,787

D. Long Term Incentive Compensation

Q. IS PUBLIC SERVICE SEEKING RECOVERY OF A PORTION OF THE LONG-TERM INCENTIVE COMPENSATION IN RATES?

A. Yes. Public Service requests recovery in base rates of $531,956 for a portion of the long-term incentive ("LTI") compensation program. In particular, Public Service seeks recovery of the performance-based component of LTI related to Xcel Energy's environmental activities, which I refer to as the "environmental component" of the LTI.

Q. PLEASE DESCRIBE THE LTI.

A. The LTI program is similar to other compensation provided by the Company in that it is intended to attract, retain, and motivate superior performance from employees. LTI, however, is different from AIP and other compensation in that is offered only to executives and other senior management employees[3]. LTI generally consists of granting: (1) executives long-term incentives both in the form of performance shares and performance-based restricted stock units; and (2) other participants long-term incentive only as performance-based restricted stock units. The performance-based restricted stock units are relevant to my testimony as they relate to the environmental component of the LTI program. Because Xcel Energy's LTI is performance based, payout of compensation only occurs when pre-defined performance goals are achieved. The performance period is three years. The performance-based restricted stock units are granted in the first year and performance is measured at the end of the third year.

Q. HOW DOES THE THREE-YEAR PERFORMANCE PERIOD IMPACT THE ACCRUAL OF LTI EXPENSE?

A. Accrual of LTI expense occurs ratably over a three year period and, therefore, reflects LTI plans in effect during each of the three years. The $531,956 Public Service requests recovery of is the actual expense the Company accrued in 2013 for the environmental component. The 2011, 2012, and 2013 plans were active plans during 2013 and therefore a portion of each plan's accrual was reflected in this amount.

Q. HOW IS THE ENVIRONMENTAL COMPONENT MEASURED FOR AWARD PAYMENT UNDER THE 2012 AND 2013 LTI PROGRAMS?

A. In 2012 and 2013 LTI Programs, performance-based restricted stock units granted for the environmental component were measured through environmental

3 Prior to 2013 the environmental LTI was only offered to executive employees. Beginning in 2013, LTI was also offered to Business Unit Vice Presidents.

projects and retail average rate ("RAR") performance ranking relative to companies included in the Edison Electric Institute ("EEI") Electric Index. The environmental projects or initiatives fall into one of two categories: (1) Renewable Energy; or (2) Emissions Reductions. Renewable Energy targets are directed toward increasing renewable energy resources on the Xcel Energy system, such as placing into commercial operation a targeted number of megawatts of Operating Company-owned renewable energy projects. Emissions Reductions targets include the retirement of plants in the fleet with the highest air emissions or the completion of capital projects that improve emissions. If the environmental goals are met, then the award level is determined using Xcel Energy's performance ranking based on the weighted average RAR relative to the other companies in the EEI Electric Index.

Q. HOW WAS THE ENVIRONMENTAL COMPONENT MEASURED FOR AWARD PAYMENT UNDER THE 2011 LTI PROGRAM?

A. In 2011, performance-based restricted stock units granted for the environmental component were measured by Xcel Energy's average annual estimated emissions reductions in millions of tons. The percentage of units awarded was based on the amount of emissions reductions achieved, with 100 percent of units awarded for a target reduction of 5 million tons.

Q. WHY IS IT REASONABLE TO GRANT RATE RECOVERY OF LTI COSTS RELATED TO THE ACCOMPLISHMENT OF ENVIRONMENTAL PROJECTS?

A. The operational-based project goals of the environmental LTI component align management's interests with Xcel Energy's long-term environmental strategy and with the interests of shareholders and customers. In particular, the achievement of the environmental LTI objectives has a direct benefit to customers and the public through prudently reducing air emissions and their impact to the environment.

Q. IS PUBLIC SERVICE SEEKING RECOVERY OF ALL LTI COSTS THROUGH RATES?

A. No. Public Service is only seeking recovery of the LTI inclusive of the environmental component. As noted by Ms. Blair, Public Service has removed more than $3.6 million from the Test Year cost of service related to LTI costs.

E. Reasonableness Of Public Service's Cash Compensation

Q. HAS XCEL ENERGY COMPARED ITS TOTAL CASH COMPENSATION LEVELS TO THE COMPETITIVE MARKET, INCLUDING OTHER UTILITIES?

A. Yes, as explained earlier, we use the median of market survey data to ensure our total cash compensation levels are consistent with the market. We also engaged Towers Watson to perform an analysis of how Xcel Energy's 2013 target total cash compensation compares with the compensation of other utility companies. A copy of the 2013 Towers Watson Compensation Study is provided as Confidential Attachment No. RKL-1. The 2013 Towers Watson Compensation Study includes exempt and executive employees.

Q. PLEASE DESCRIBE THE SPECIFIC ELEMENTS OF THE 2013 TOWERS WATSON COMPENSATION STUDY.

A. The 2013 Towers Watson Compensation Study consists of the following elements:

- Xcel Energy's total cash compensation levels (total cash compensation is defined as base salary plus target annual incentive compensation) were compared with competitive market target total cash compensation levels;
- Xcel Energy's base salary levels were compared with competitive market total cash compensation levels; and
- Xcel Energy's annual incentive targets were compared with market annual incentive targets.

The 2013 Towers Watson Compensation Study compared Xcel Energy's level of compensation to the median and average levels of compensation paid by the comparison groups.

Q. WHAT COMPARISON GROUPS DID THE 2013 TOWERS WATSON COMPENSATION STUDY USE?

A. Compensation levels were compared with two sets of data. The first set of comparison data was national data reflecting a large majority of investor-owned utilities including those both smaller and larger than Xcel Energy. The second set of comparison data was of investor-owned utilities similar in size to Xcel Energy. The second set of data is significant because it includes only larger companies. Managerial positions in larger organizations typically have greater complexity and therefore require more skill, which in turn increases the compensation requirements.

Q. WHAT WERE THE RESULTS OF THE 2013 TOWERS WATSON COMPENSATION STUDY?

A. As shown on Table 8, the Towers Watson study finds that with the inclusion of the AIP, Public Service's median total cash compensation levels are generally in line with other utilities. Without the AIP, however, the median total cash compensation provided would be well below the overall utility market and would put us at a material disadvantage in the competition for talented employees.

Table 8

Components of Xcel Energy Compensation	**Compared to Base Salaries and Incentives of Utilities with Similar Revenues (Revenue Sample)**	**Compared to Base Salaries and Incentives of Utilities Across the Nation (National Sample)**
Base Salary Only	Below Market By 15.6%	Below Market By 12.2%
Target Total Cash Compensation (Base Salary + Target Incentive)	Below Market by 4.0%	Above Market by 0.7%

Q. WHAT DO YOU CONCLUDE FROM THE 2013 TOWERS WATSON COMPENSATION STUDY?

A. The Towers Watson Compensation Study validates that Xcel Energy's compensation structure (i.e., both base salary and the AIP) provides a market level of compensation, which confirms that Public Service's requested compensation expense is appropriate and reasonable. The study also confirms that the target level annual incentives provided to employees through the AIP are aligned with those for similar positions in the competitive market. Without the AIP, however, our total cash compensation would lag the market by 15.6 percent (compared to utilities with similar revenues), which would put Public Service at a material disadvantage when competing for skilled employees.

Q. DID THE 2013 TOWERS WATSON COMPENSATION STUDY INCLUDE CONSIDERATION OF THE LTI ENVIRONMENTAL COMPONENT THAT PUBLIC SERVICE SEEKS RECOVERY OF IN RATES?

A. No. However, as noted earlier, only executives and Business Unit Vice Presidents participate in the environmental component of the LTI.

Q. IS THE 2013 TOWERS WATSON COMPENSATION STUDY THE ONLY STUDY THE COMPANY RELIES UPON FOR PURPOSES OF BENCHMARKING ITS TOTAL CASH COMPENSATION LEVELS?

A. No. As noted above, the Company routinely uses a number of additional third-party surveys to compare its total cash compensation levels and programs to those of other firms, including both other utilities and non-utilities. The Company uses the median of this data to ensure its total cash compensation is comparable to the market.

Q. ARE XCEL ENERGY'S BASE SALARY AND ANNUAL INCENTIVE COMPENSATION PROGRAMS NECESSARY AND REASONABLE?

A. Yes. Public Service and Xcel Energy must provide a market-competitive level of total compensation to attract and retain the employees who in turn provide safe and reliable electric service to Public Service's customers. A base salary coupled with the AIP, and recognition programs is an appropriate method of providing market competitive total cash compensation.

IV. EMPLOYEE HEALTH & WELFARE BENEFIT PROGRAM

Q. PLEASE BRIEFLY SUMMARIZE THE FEATURES OF XCEL ENERGY'S HEALTH AND WELFARE BENEFITS PROGRAMS.

A. The Company's employee health and welfare programs primarily consist of providing medical, pharmaceutical, dental, vision, disability, and life insurance coverage to our non-bargaining and bargaining employees and their families.

Q. HAS XCEL ENERGY UNDERTAKEN ANY INITIATIVES TO SLOW THE RATE OF GROWTH IN HEALTH AND WELFARE RELATED BENEFIT COSTS?

A. Yes. Over the past several years, Xcel Energy has made several design changes and undertaken an array of initiatives to help mitigate health care costs. Many of these initiatives have resulted in a greater share of healthcare costs being borne by employees, but they have also allowed Xcel Energy to better manage overall healthcare costs and the rate at which costs increase. These initiatives include:

- Reducing the number of health insurance plans available to non-bargaining employees from four to one. Since 2009, the only medical plan that Xcel Energy has made available to non-bargaining employees is the High Deductible Health Plan ("HDHP"). This helps to manage overall plan costs by increasing employee awareness of medical costs.
- Beginning in 2011, Xcel Energy increased employees' out-of-pocket costs in the HDHP by introducing co-insurance, which means that even after meeting their high deductible, employees continue to pay co-insurance on additional medical and pharmacy claims up to $3,500 per individual or $7,000 per family.
- Beginning in 2011, Xcel Energy implemented pharmacy cost-containment programs that require non-bargaining employees to pay additional out-of-pocket expenses if they choose to purchase drugs in a less cost-effective manner.
- In 2012, Xcel Energy re-introduced a monthly employee premium under the HDHP.

- In 2010, adult orthodontia coverage was eliminated from the non-bargaining dental plan.
- In 2011, the Short-Term Disability program was reduced from 100 percent income replacement for 26 weeks to 100 percent for the first 13 weeks, and then 70 percent of income replacement for the remaining 13 weeks.
- In 2012, Xcel Energy launched a new wellness program, *My Health Choices* for non-bargaining employees. It encourages employees and their spouses to understand their current health status and make better decisions about their health by providing a contribution to a Health Savings Account ("HSA") for employees who are healthy or trying to become healthier. Those that choose not to engage in the program ultimately pay more for medical coverage.
- Vendor contracts are continually monitored and renegotiated with benefit vendors on an ongoing basis. These negotiations focus on administrative fee reductions, better performance guarantees and rebates, and improved discounts on provider networks. All contribute to our ability to mitigate the increasing healthcare costs and benefit administration costs charged by third parties.
- Xcel Energy recently completed a thorough evaluation of the healthcare options available to Medicare-eligible retirees through the individual market related to medical and prescription drug coverage, and we found that those plans provide broad, comprehensive coverage at affordable costs. Therefore, we took a new approach effective Jan. 1, 2013 to transition our non-bargaining Medicare-eligible retirees and their Medicare-eligible spouses and dependents from the Company plan options to the individual market. This reduced the Company's financial liability and administrative responsibilities, and it gave us the opportunity for significant cost savings for retiree groups that still had premium subsidies.

Q. DESPITE THE INITIATIVES UNDERTAKEN TO HELP MITIGATE INCREASES IN HEALTH CARE COSTS, IS PUBLIC SERVICE STILL EXPERIENCING INCREASES IN HEALTH CARE COSTS?

A. Yes. As noted by Company witness Mr. Richard Schrubbe, Xcel Energy anticipates experiencing a medical inflation rate of approximately 7.0 percent for 2014 and 2015. This is a trend that Xcel Energy expects to continue over the duration of the proposed Test Year. Mr. Schrubbe supports the reasonableness of the 7.0 percent medical inflation rate.

Q. ARE XCEL ENERGY'S BENEFITS PROGRAMS AND THEIR COSTS NECESSARY AND REASONABLE?

A. Yes. Xcel Energy designs programs that promote a culture of personal accountability for employees' physical and financial well-being, while ensuring the long-term financial health of our programs. Xcel Energy provides competitive benefit programs that are necessary to attract and retain a qualified, skilled workforce. Based upon my experience designing, implementing, and administering benefits plans, and my familiarity with corporate benefits practices, Xcel Energy's benefit plans are reasonable, appropriate, and competitive with what is provided by the market.

V. XCEL ENERGY'S EMPLOYEE RETIREMENT PROGRAM

Q. PLEASE BRIEFLY SUMMARIZE THE FEATURES OF XCEL ENERGY'S RETIREMENT PROGRAMS.

A. Xcel Energy provides retirement benefits to eligible employees, which include a defined benefit (pension) plan, as well as a defined contribution (401(k)) savings plan. Xcel Energy's pension or defined benefit programs are non-contributory programs (*i.e.*, programs to which employees do not contribute), which provide pay replacement to eligible employees after separation of service. The 401(k) savings plan encourages employees to save regularly and cost effectively for their retirement through pre-tax and after-tax employee deferrals and provides an employer matching contribution up to a maximum amount. The amount of the employer contribution differs based upon the 401(k) plan for which the employee is eligible.

A. DEFINED BENEFIT PLAN

Q. IS IT COMMON IN THE UTILITY INDUSTRY TO HAVE A DEFINED BENEFIT PLAN?

A. Yes, it is very common. Of the 48 utilities in the Fortune 1000, 32 (67 percent) continue to provide defined benefit pension benefits to all employees, 13 (27 percent) provide defined benefit pension benefits to all employees except those hired after a certain date, and only three have fully or partially discontinued the defined benefit pension benefit for employees.[4]

4 Information gathered from annual reports for the Fortune 1000 utilities.

Q. HAS THE COMPANY UNDERTAKEN ANY INITIATIVES TO REDUCE THE COSTS OF ITS DEFINED BENEFIT PENSION EXPENSE?

A. Yes. Effective January 1, 2012, non-bargaining new hires and rehired employees are no longer eligible for the 10% Pension Equity Plan ("PEP"). Instead, these employees participate in a 5% Cash Balance Plan formula without pension supplements (*i.e.,* Retirement Savings Account or Social Security Supplement).

In addition, Xcel Energy has previously implemented benefit level reductions for our Public Service bargaining unit employees by reducing the multiplier for newly hired employees effective in 2010, and changed the final average compensation definition from 36 months to 48 months, effective January 1, 2012 for all bargaining unit employees.

As discussed by Company witness Mr. Schrubbe, the plan design changes have reduced the level of pension cost that the Company seeks recovery of during the Test Year.

Q. PLEASE DESCRIBE THE CASH BALANCE PLAN FORMULA.

A. The 5% Cash Balance Plan provides for an annual 5 percent Company contribution of the employee's annual salary into a notional account. This account has interest credited to it annually based on the 30-year Treasury rates. Because the value of the plan is expressed in dollars, the 5% Cash Balance Plan looks similar to a savings account or a 401(k) plan, so employees easily understand the plan value. Non-bargaining employees hired prior to January 1, 2012 are eligible for the 10% Pension Equity Plan, which results in employees receiving 10 percent of their highest 48 months of consecutive earnings for each year of eligible service.

B. Defined Contribution Plan

Q. PLEASE DESCRIBE THE COMPANY'S DEFINED CONTRIBUTION PLAN.

A. The Company's defined contribution plan, which is a 401(k) savings plan, provides an employer contribution equal to a maximum of 4 percent of an employee's eligible compensation (i.e., base salary). The Company matches 50 cents on the dollar up to 8 percent of a non-bargaining employee's contribution. For bargaining unit employees, the Company provides a 5 percent match on eligible compensation.

Q. WHY IS IT REASONABLE FOR 401(K) EXPENSE TO BE INCLUDED IN RATES?

A. The expense is reasonable not only because it is an important part of our benefit program to attract and retain talent, but as stated in the Direct Testimony of Mr. David Pitts of Moody's Analytics from Proceeding No. 12AL-1268G, the combination of the Company's 5% Cash Balance Plan and 401(k) savings plan provides a *lower* benefit than what is offered by other regulated utilities. As discussed more fully below, this conclusion was part of a Joint Pension Study performed by Mr. Pitts pursuant to a settlement agreement in Proceeding No. 11AL-947E. Mr. Pitts' Direct Testimony from Proceeding No. 12AL-1268G addressed the Joint Pension Study and is provided as Attachment No. RKL-2. A copy of the Joint Pension Study is provided as Attachment No. RKL-3.

C. REASONABLENESS OF PUBLIC SERVICE'S RETIREMENT BENEFITS

Q. IS IT NECESSARY TO CONSIDER BOTH THE DEFINED BENEFIT PLAN (PENSION) AND THE DEFINED CONTRIBUTION PLAN (401(K)) WHEN THE COMMISSION CONSIDERS THE REASONABLENESS OF THE COMPANY'S RETIREMENT PROGRAM AS A WHOLE?

A. Yes. It is important to compare programs holistically because the competitive market offers varying combinations of retirement programs including a combination of pension and 401(k) plans. The Company offers a cost effective program by maintaining a pension benefit; giving employees some stability with a portion of their future income, while also offering a 401(k), which allows employees to increase their overall retirement savings.

Q. DOES THE COMPANY'S PENSION PLAN REPRESENT A REASONABLE LEVEL OF BENEFITS?

A. Yes. Our pension levels, historically and currently, represent a reasonable level of benefits. Alignment with what the external market is offering for a pension benefit is a major component of our pension plan design.

D. JOINT PENSION STUDY

Q. DID THE COMPANY COMMISSION A STUDY OF THE REASONABLENESS OF THE PENSION PLAN PROVIDED TO NEWLY HIRED EMPLOYEES AS AGREED TO IN THE SETTLEMENT AGREEMENT ENTERED INTO IN PROCEEDING NO. 11AL-947E.

A. Yes. In Proceeding No. 11AL-947E, a settlement agreement was reached which included a requirement that Public Service engage an independent consultant to evaluate the reasonableness of pension benefits provided by Xcel Energy to new hire non-bargaining unit employees of either Public Service or Xcel Energy Services Inc. at the time of the study, as compared to such benefits provided by corporations comparable to Xcel Energy, Inc. and to corporations of similar size outside the utility industry with employees of similar job titles and responsibilities.[5] As required under the Settlement Agreement, the Staff and Public Service engaged David Pitts of Moody's Analytics to conduct the Joint Pension Study.

Q. HAS MR. PITTS PROVIDED TESTIMONY TO DISCUSS THE APPROACH, ASSUMPTIONS, VALUATION METHODOLOGY, AND DATA USED FOR THE JOINT PENSION STUDY?

A. Yes, Mr. Pitts' Direct Testimony from Proceeding No. 12AL-1268G provided this discussion.

Q. WHAT WERE THE RESULTS OF THE JOINT PENSION STUDY?

A. As discussed in the Direct Testimony of Mr. Pitts from Proceeding No. 12AL-1268G, the key findings of the Joint Pension Study are:

- Public Service has effectively implemented changes in its retirement plans which significantly reduce the cost of benefits for non-bargained new hires.
- Public Service has implemented changes in its investment policies to more effectively control the volatility of pension expense, which will mitigate unpleasant surprises in pension expense, minimum required cash contributions, and retirement benefit expenses submitted for reimbursement by ratepayers.

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5 *See* Section 11 of the Settlement Agreement.

- Benefits being provided to non-bargained, new hire employees are in the bottom twentieth percentile of comparable benefits for regulated utilities, and equal to the average of benefits being provided by non-regulated utilities.
- Although the new hire benefits are significantly less than those provided to legacy employees, a full career employee saving 8 percent of his earnings per year is expected to generate sufficient retirement wealth through personal savings, Social Security, and Public Service retirement contributions, to be able to retire without suffering a reduction in standard of living.
- Public Service has implemented effective cost control measures for new hires, but it will take several years to fully realize the benefits of those savings. Limiting the grandfathered group to a smaller subset of the population would have accelerated the cost savings.

Q. DO YOU HAVE A RESPONSE TO THE KEY FINDINGS OF THE JOINT PENSION STUDY?

A. In general I interpret the Joint Pension Study as supporting the efforts Xcel Energy undertook through the 5% Cash Balance Plan for new non-bargaining hires and shows the pension plan is comparable with or below what is offered by regulated and non-regulated utilities. Thus, the Joint Pension Study generally supports the pension plan's reasonableness. With respect to the finding that further savings could have been achieved if the Company had enacted the new plan for all non-bargaining employees[6], the Company's decision to draw the line at new-hires was based on consideration of a number of factors, including the impacts on our employees and the financial impact to our business. We also considered the practices of other utilities, the effect on potential unionization, and the legal risks. Xcel Energy ultimately decided to limit the new plan to new hires after January 1, 2012 for several reasons.

- *Disruption to existing employees.* Like many utilities, a significant portion of our highly skilled workforce is already eligible to retire or very close to retirement. Changing the pension benefits for these employees would increase the risk of them leaving earlier, resulting in a significant loss of necessary knowledge to run our business. Unplanned early retirements pose concerns due to our specialized skill sets, supply of viable candidates, and the need for a seamless knowledge transition.
- *Complexity.* Changing benefits for existing employees involves significant transition rules required under the laws governing qualified pension plans. These transitions increase costs to communicate and administer the benefits.
- *Unionization risk.* Changes to the bargaining unit pension plan must be negotiated, and making a change to existing employee's non-bargaining pension benefit in absence of similar changes to the bargaining group could result in employee unionization and the added costs associated with it.

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6 *See* page 7 of the Joint Pension Study.

- *Financial considerations.* Our analysis demonstrated that projected cost savings were not significant enough to offset this risk. Our attrition rate, which was previously discussed, has been rising as a result of our aging population and the number of employees eligible to retire. As more non-bargaining employees are retiring and replacement employees are going into the 5% Cash Balance Plan, we knew we could achieve our benefit objectives more effectively by simply making the change for new hires.
- *Market practice.* It is a common practice for employers when making changes to their retirement offerings to eliminate or reduce defined benefit pension plan benefits for new hires only. Based on a Towers Watson study of pension changes in the last decade, 48 percent of defined benefit plan sponsors significantly changed their program for current employees at some point in the last 10 years. However, the prevalence is considerably different within the utility industry, which showed only 34 percent of utilities significantly change their programs for current employees.[7]

This business decision eliminated the complexity and disruption associated with changing an employee's existing vested benefit, as well as allowing us to achieve our financial objectives.

7 Towers Watson, "Pensions in Transition: Retirement Plan Changes and Employer Motivations," 2012.

VI. CONCLUSION

Q. ARE THE 2015 O&M COSTS FOR THE TOTAL REWARD PROGRAM YOU DESCRIBE ABOVE REFLECTED IN THE TEST YEAR COST OF SERVICE PRESENTED BY MS. BLAIR?

A. Yes. The 2015 level of O&M for the Total Rewards Program presented in my testimony are necessary to attract, engage, and retain the employees needed to provide safe and reliable service to our customers and therefore a reasonable input into the Test Year Cost of Service.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

Attachment A
Statement of Qualifications
Ruth K. Lowenthal

I received my Bachelor of Arts degree in Government & Politics from the University of Maryland and my Juris Doctor degree from the University of Maryland School of Law. I also have Certified Compensation Professional and Certified Benefits Professional designations from WorldatWork.

My current position with Xcel Energy Services is Senior Director, Total Rewards. In my current role, I have responsibility for Employee Benefits for Retirement and Health and Welfare, Compensation, Payroll, and HR Operations. I provide leadership and have strategic responsibility for designing, developing, and implementing a Total Rewards Program that aligns with other employers with who Public Service competes for employees and enhances Xcel Energy’s ability to attract, motivate, and retain talent at all levels through the organization. In addition, I am responsible for ensuring that our HR programs and services are administered accurately, cost-effectively, and efficiently. I have been employed by Xcel Energy in my current position since 2011.

Before coming to Xcel Energy Services I was employed by Target Corporation for twenty years with various positions including Director of Human Resources, Analytics, and Business Intelligence; Director of Human Resources, Strategy; Director of Benefits; and Director of Executive Compensation. Before serving in Target’s Human Resources Department, I was an attorney at Target. Among other things, I was responsible for directing a team that provided legal counsel to management on a wide range of benefits, compensation, and other business matters including FMLA, ERISA, HIPAA, ADA and other business matters.

Confidential Attachment No. RKL-1

(Towers Watson Compensation Study)

Filed under seal

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

DOCKET NO. 12AL-1268G

IN THE MATTER OF ADVICE LETTER NO. 830 - GAS OF PUBLIC SERVICE COMPANY OF COLORADO, WITH ACCOMPANYING TARIFF SHEETS CONCERNING IMPLEMENTING A GENERAL RATE SCHEDULE ADJUSTMENT (GRSA), TO BECOME EFFECTIVE JANUARY 12, 2013.

PENSION STUDY TESTIMONY OF DAVID PITTS
ON BEHALF OF
STAFF OF THE COLORADO PUBLIC UTILITIES COMMISSION

April 26, 2013

TABLE OF CONTENTS

EXHIBIT DGP-6 (35 PAGES)

I. INTRODUCTION AND PURPOSE OF TESTIMONY

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is David Pitts. My business address is 7 World Trade Center, 250 Greenwich Street, New York, NY 10007.

Q. HAVE YOU PREVIOUSLY FILED TESTIMONY IN DOCKET NO. 12AL-1268G?

A. Yes. On April 3, 2013, I filed Answer Testimony on behalf of Staff of the Public Utilities Commission (Staff). Moody's Analytics was engaged by Staff to perform a review of the level of retirement benefits being provided to *all employees as of today,* with related impact on overall corporate financials (Comprehensive Study of PSCo Retirement Benefits or "Comprehensive Study"). My Answer Testimony included the results of this review. I note Appendix A to my Answer Testimony includes a statement of my experience and qualifications.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is to present the results of the Pension Study referenced in my Answer Testimony filed April 3, 2013. I make no specific recommendations in this Testimony.

II. PENSION STUDY

Q. WHAT ARE THE MAIN OBJECTIVES OF THE PENSION STUDY OF PSCO RETIREMENT BENEFITS?

A. Moody's Analytics was engaged by PSCo and Staff to perform an independent review of the level of retirement benefits being provided to non-bargained, new hires.

The Pension Study clarifies the future cost trends, the speed in which the current cost structure will converge to the new structure, the comparability analysis between PSCo and other companies, and the relative competitiveness of PSCo's benefits for non-bargained new hire employees.

Q. DESCRIBE YOUR OVERALL APPROACH TO PERFORMING THE ANALYSIS.

A. We went through an initial scoping exercise with PSCo and Staff to identify the appropriate survey objectives and techniques. With input from PSCo and Staff, we identified a target group of companies to solicit, with an overall objective of 30 respondents spread among different sectors (regulated, non-regulated and other).

Moody's Analytics then conducted a phone and email campaign to encourage survey participation. Companies agreeing to participate were provided with a link to an electronic survey. Alternatively, participants could provide responses verbally or via other electronic means (such as providing copies of relevant employee booklets or communications).

Moody's Analytics compiled all survey responses, reviewing and supplementing as needed through follow up phone calls or additional research.

We worked directly with PSCo's actuaries to obtain the necessary actuarial assumptions relating to turnover, retirement, disability, salary progression, and mortality, which enabled us to perform the necessary projections for our study.

Q. DESCRIBE THE DATA SOURCES USED IN YOUR STUDY.

A. Plan level information on benefit formulas was provided directly by the survey respondents. A summary of relevant pricing information by company and plan is included in Table 1 of the attached **Exhibit DGP-6**.

Participant level data was provided directly by PSCo, which included date of birth, date of hire, date of rehire, date of termination, and 2012 compensation and 401(k) salary deferrals. Data was submitted separately for PSCo employees and Xcel Shared Service employees. No individuals were identified by name in the data submission.

Q: DESCRIBE THE VALUATION METHODOLOGY AND ASSUMPTIONS USED IN YOUR ANALYSIS.

A: Our analysis included two different types of valuation – the development of the per capita retirement costs as a percent of payroll (Charts 1-R, 1-U and 1-O in **Exhibit DGP-6**), and the projection of retirement wealth as a multiple of final pay (Charts 3-F, 3-M and 3-E in **Exhibit DGP-6**).

The per capita Defined Benefit retirement costs were developed by first projecting the overall demographics of the company to determine a "steady-state" employee distribution. We relied on the actuarial assumptions currently used by PSCo's actuaries in performing this projection. We then priced the cash balance plan for this steady-state population, assuming a 2% spread between crediting and discounting rates. The per capita costs for other companies were calculated relative to the PSCo per capita by examining plan differences and developing suitable relative value factors.

The per capita Defined Contribution costs were developed by examining the actual savings participation rates of PSCo and Xcel, and then calculating the employer match and non-elective contributions for other company plans assuming similar savings patterns. In one instance (company R-K in Table 4 of attached **Exhibit DGP-6**), we increased the savings participation rates, as the 401(k) plan match of 200% of deferral was sufficiently generous to incent changes in savings patterns.

For the wealth projection exhibits, we relied on 1,000 simulations of the B&H ESG, with a multi-year calibration target using market conditions as of December 31, 2012. Each scenario led to a unique projection of assets and annuity purchase rates, which were then used to determine the amount of retirement wealth as a multiple of final pay, as illustrated in Charts 3-F, 3-M and 3-E in the attached **Exhibit DGP-6**.

Q: WHAT ARE THE KEY FINDINGS FROM YOUR STUDY?

A: PSCo has effectively implemented changes in its retirement plans which <u>significantly</u> reduce the cost of benefits for non-bargained new hires. Our previous study concluded legacy employees were earning retirement benefits at the rate of $15,000 per year; non-bargained new hires will earn only $5,300 per year. As we saw in the last study, PSCo has implemented changes in its investment policies to more effectively control the <u>volatility</u> of pension expense, which will mitigate unpleasant surprises in pension expense, minimum required cash contributions, and retirement benefit expenses submitted for reimbursement by ratepayers.

The benefits being provided to non-bargained, new hire employees are in the bottom twentieth percentile of comparable benefits for regulated utilities, and equal to the average of benefits being provided by non-regulated utilities. These benefits continue to exceed the average level of benefits available in other sectors of the economy.

Although the new hire benefits are significantly less than those provided to legacy employees, a full career employee saving 8% of his earnings per year is *expected* to generate sufficient retirement wealth through personal savings, Social Security, and PSCo retirement contributions, to be able to retire without suffering a reduction in standard of living. There are significant risks in achieving this goal, however. Employees in general do not save enough (PSCo's population only saves an average of 6% for example even though 8% is required to receive a full match). Furthermore, employees are now subject to much more financial risk than ever, as more of their retirement wealth will come from savings plans subject to market risk.

Whereas the new plan is lean, requiring significant contributions and investment discipline from new hires, the legacy plan provides sufficient retirement income for employees to enable them to retire at age 61, on average. The transition approach adopted by PSCo – namely to simultaneously sponsor two separate structures for legacy employees and new hires – means there will be two different classes of employees for as long as the next 40 years or so.

PSCo has implemented effective cost control measures for new hires, but it will take several years to fully realize the benefits of those savings. The demographic projections illustrated in Charts 2-P and 2-X of **Exhibit DGP-6** suggest that almost one-fourth of the population will still be accruing benefits under the legacy formula in 10 years time. Limiting the grandfathered group to a smaller subset of the population (all employees over age 45 at 12/31/2011, for example – about 2/3 of the population) would have accelerated the cost savings.

Q. DOES THIS CONCLUDE YOUR TESTIMONY AT THIS TIME?

A. Yes.

Moody's
Analytics

Custom Retirement Benefit Survey

Performed on behalf of Public Service Company and Colorado Public Utilities Commission

David G. Pitts, FSA, MAAA **Director, Product Specialist**

April 2013

Introduction

Moody's Analytics was hired by the Public Service Company of Colorado (PSCo) and the Colorado Public Utility Commission (PUC) to perform an independent survey of retirement benefits.

The objective of the survey was to provide PSCo and the PUC with sufficient information to help them determine whether the retirement benefits being provided for PSCo's non-bargained, new hire population are reasonable and just.

Our survey focused on defined benefit and defined contribution plans sponsored in three different sectors: regulated utilities, non-regulated utilities, and other (non-utility) companies. We did not consider retiree medical or any other post-employment benefit plans in our analysis. Our focus was on plan structures for non-bargained, new hires as of the date of the study.

We performed a custom survey by first identifying several hundred possible survey candidates representing the aforementioned sectors. Next we engaged in a phone and email campaign to incent participation, with 31 companies ultimately agreeing to participate. Plan data was obtained through an electronic survey or verbally upon request.

The remainder of this report summarizes our key findings, and includes relevant observations identified in our prior Comprehensive Study performed on behalf of the PUC and submitted in earlier testimony.

Key Findings

The financial crises in 2002 and then again in 2008 helped to accelerate three general trends within the corporate sector relating to retirement plans:

- Defined Benefit (DB) promises were modified, eliminating “final pay” type benefit structures with lucrative early retirement provisions
  - Although these modifications could legally be imposed on all employees, in practice most companies opted to make changes directly to new hires, with some form of transition credit or grandfathering for existing employees (“legacy employees”).
  - Transition credits and grandfathering is generally limited to a select group of employees – those most affected by plan changes, closest to retirement, and least able to make significant changes in their retirement planning
- Defined Contribution (DC) plans or structures became the retirement benefit of choice for most employers
  - This change shifts longevity and financial risk from the employer directly to the employee.
- Governance for DB plans has evolved to include a risk-based focus
  - The financial crises underscored the risk to the employer of investing pension assets in a manner inconsistent with benefit liabilities.

Key Findings

Consistent with these overall trends, PSCo made several changes to its plans:

- The DB plan was changed for non-bargained new hires
  - Non-bargained new hires are no longer covered under the final pay formula. Instead, they are covered under a cash balance formula, with annual pay credits equal to 5% of pay and interest credits based on the 30 year treasury rate as of the prior November.
  - Anecdotally (we did not directly survey this feature), PSCo appears to have given generous grandfathering status to any employee hired before 2012. As indicated earlier, many employers limit the grandfathered group to those most affected by a plan change
- The DC plan includes auto-enrollment and auto-escalation features to improve participation levels
  - Employees are automatically enrolled in the 401(k) plan upon hire at a 4% deferral rate. The deferral rate is automatically increased by 1% annually, until a 10% savings rate is achieved. (Employees have the ability to opt-out of these salary deferrals, but must affirmatively elect to do so.)
- DB plan investment strategy was changed
  - As revealed in the Comprehensive Study, PSCo has adopted a liability-driven type investment strategy which helps to control overall financial volatility

Key Findings

Financials

The subject of pension finance is a complicated one, as there are several valuation bases of interest, including statutory funding under ERISA, financial reporting under GAAP, and pension buy-out as evidenced by risk transfer pricing inherent in the growing annuity purchase market (e.g., the GM and Verizon risk transfer deals.)

Furthermore, pension cost includes both operating costs (the value of benefits being earned by employees) as well as financing costs (amortization costs/credits for funding deficits/surpluses).

- For purposes of this analysis, we are focusing on the operating costs, as these are representative of the value of benefits being earned by employees.

- The financing cost is related to the current funded status of the pension plan. Many practitioners (including Moody's Investor Services) consider the pension deficit as an overall debt of the corporation.
  - The most recent 10-k filed by PSCo suggests a pension deficit of $139 million as of 12/31/2012 calculated on an accounting (GAAP) basis
  - On a buy-out basis, this deficit could easily be $300 million or more

Key Findings

Financials

We estimate the “steady-state” operating retirement costs for PSCo non-bargained, new hires at 7% of payroll.

- The steady-state cost represents the ultimate level of costs the new hire population will experience. Current costs for this group are lower, as the new entrant population is young (and growing)
- As shown in Charts 1-R, 1-U and 1-O, the PSCo retirement operating costs for non-bargained, new hire employees are:
  - In the bottom 20%-ile of regulated utilities
  - At the median of non-regulated utilities
  - Well above the median for other companies

Key Findings

Financials

We next looked at the estimated impact of the plan change on the operating costs for PSCo as a whole.

- Charts 2-P and 2-XS demonstrate the projected proportion of PSCo's active employee group that could be considered "legacy" employees vs. "new hires". The legacy employees continue to accrue retirement benefits under the old plan, whereas the new hires earn benefits under the new plan.
- As indicated in the prior Comprehensive Study, the per-capita retirement costs for legacy employees is approximately $15,000 per year. The current study concludes that the per-capita retirement costs for new hires is $5,300 per year.
- As developed in Table 1:
  - The "old plan" would have generated $289 million in operating costs over a 5 year period
  - The new plan is expected to generate $269 million in operating costs over a 5 year period, a savings of $20 million
  - Had the new plan been enacted for all non-bargained employees, the 5 year operating costs would have been $199 million, a savings of $90 million over the prior plan

Key Findings

Individual Employee Impacts

We also compared the retirement benefit accumulation and adequacy for PSCo vs. others in the regulated utility sector.

- Chart 3-F illustrates the accumulated retirement wealth under both the DB and DC plans for a Full Career Employee (hired at 25 / retires at 65).
- Chart 3-M examines similar values for a Mid Career transfer (hired at 50 / retires at 65).
- Chart 3-E considers an Early Leaver (hired at 25 / leaves at 35).

Conclusions:

- The overall ranking for PSCo's projected benefits under each sample employee is similar to the overall per-capita results which indicated bottom 20%-ile
- Compared to other regulated utilities, PSCo tends to favor Early Leavers over Mid Career Transfers. This is a function of the age / service weighted pay credits prevalent in most other companies but not in PSCo

Key Findings

Individual Employee Impacts

Conclusions (continued):

- The projected retirement wealth for a full career employee at PSCo appears to be sufficient for a reasonable retirement income
  - The median expected retirement wealth for a full career employee is about 10 times final salary
  - Social Security represents about 3 times final salary for many employees, bringing total retirement wealth to 13 times final pay – considered sufficient by many experts to sustain a comparable standard of living in retirement to that enjoyed during working years
- There are two important caveats
  - The employee must contribute a full 8% of pay each and every year over a 40 year time horizon to meet this target
  - There is significant volatility in this projection
    - In 1 in 4 instances, the retirement wealth is as low as 8 times pay
    - In 1 in 20 instances, the retirement wealth is as low as 6 times pay
    - Such outcomes will lead to delayed retirements and less orderly workforce transition for the employer

Additional Findings

Prevalence Statistics

As observed in Table 2, regulated utilities seem to lag non-regulated utilities to some degree in implementing pension cost / risk control features, and other companies to a greater degree

- 3 out of 14 regulated utilities still sponsor final pay pension plans, compared to 1 out of 8 non-regulated companies, and 0 out of 9 other companies

Employer Stock

PSCo is the only company that continues to provide its company matching 401(k) contribution in employer stock.

- Most companies have eliminated this practice because of fiduciary liability (stock-drop lawsuits).
- Many investment professionals would also suggest diversifying this risk. The employee's salary (which can't be diversified) is already tied to the success of the company.

Additional Findings

Auto-enrollment / escalation

Although most companies provide auto-enrollment and escalation features (see Table 4), most experts suggest employees need to save significantly more than they currently are.

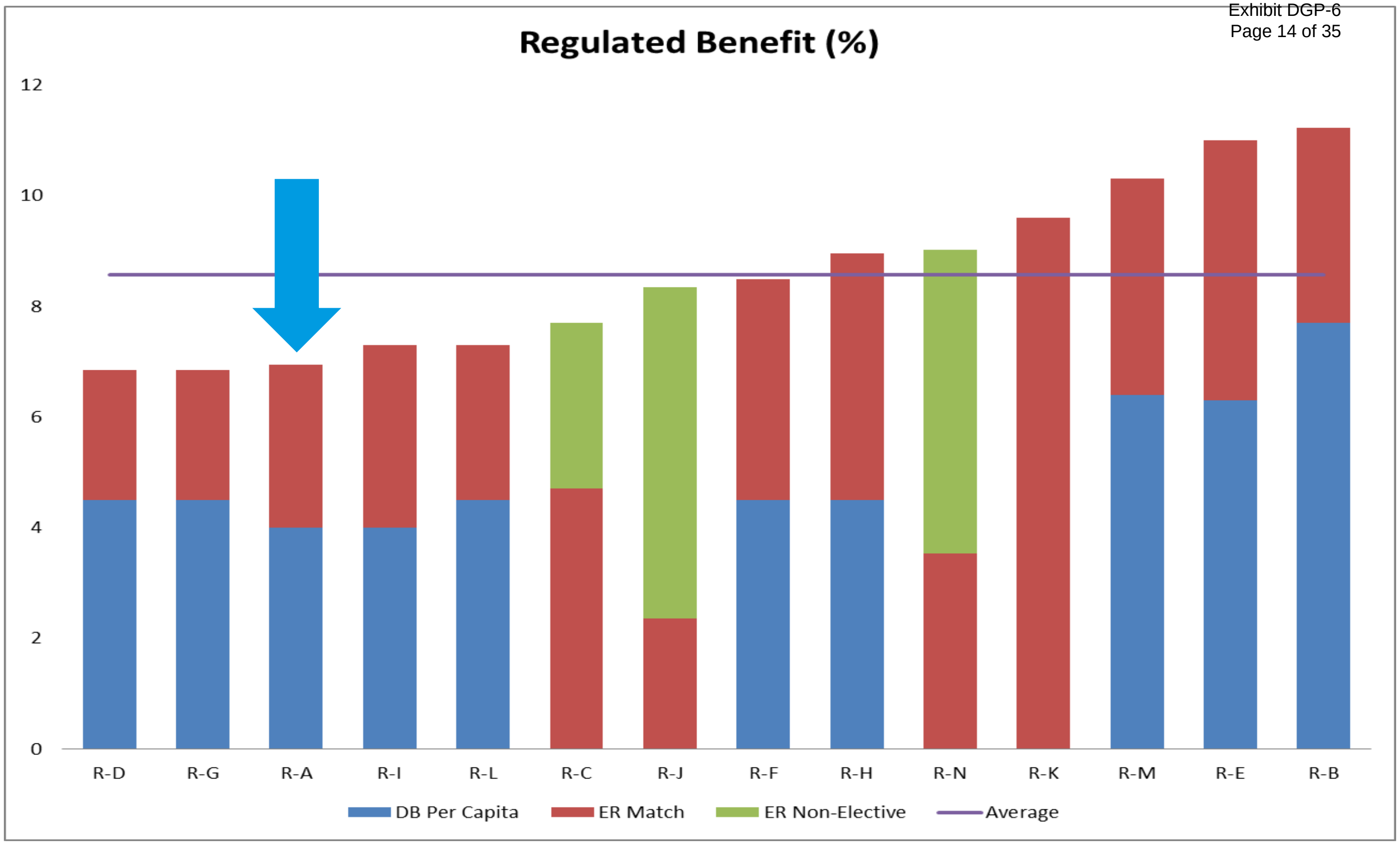
- Stopping auto-escalation features at the level which provides the full employer match (company U-A for example) gives an implicit message to employees that they don't need to contribute more to their retirement savings
- Company R-K provides the best example for incenting retirement savings, which includes auto-escalation features until an employee reaches a savings rate of 19% of pay

Exhibits

Guide to Exhibits

Charts	Description	Tables	Description
1-R	Per capita cost comparison - Regulated	1	Operational Cost Projections
1-U	Per capita cost comparison - Unregulated	2	Prevalence Statistics
1-O	Per capita cost comparison - Other	3	Survey Participants
2-P	PSCo Demographic Projection	4	Detailed Plan Summaries
2-X	XS Demographic Projection		
3-F	Retirement Wealth Projection – Full Career		
3-M	Retirement Wealth Projection – Mid Career Transfer		
3-E	Retirement Wealth Projection – Early Leaver		

Chart 1-R: New Hire Retirement Costs As a % of Payroll Regulated Utilities



MOODY'S ANALYTICS

Chart 1-U: New Hire Retirement Costs As a % of Payroll Unregulated Utilities

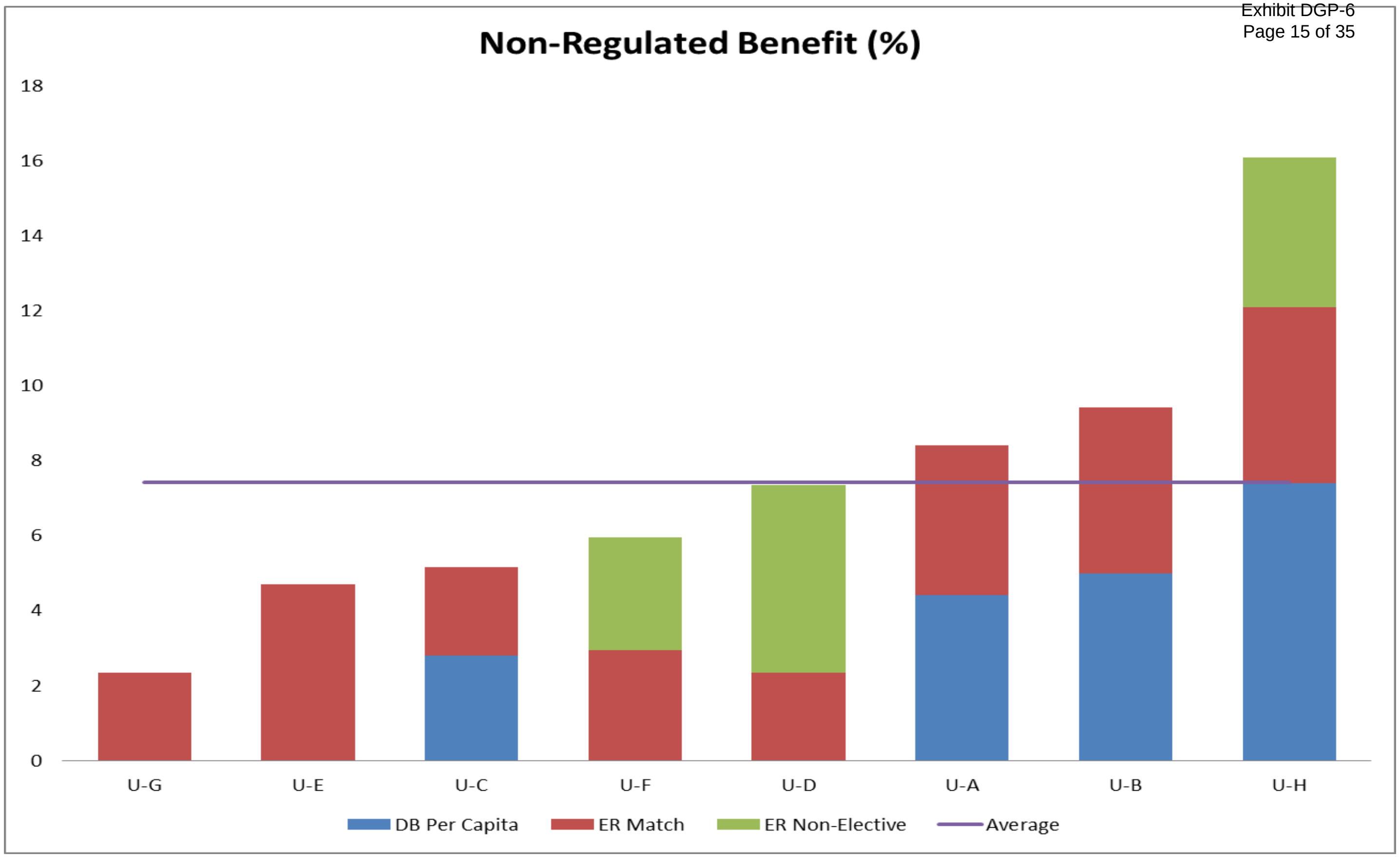


Chart 1-O: New Hire Retirement Costs As a % of Payroll Other Companies

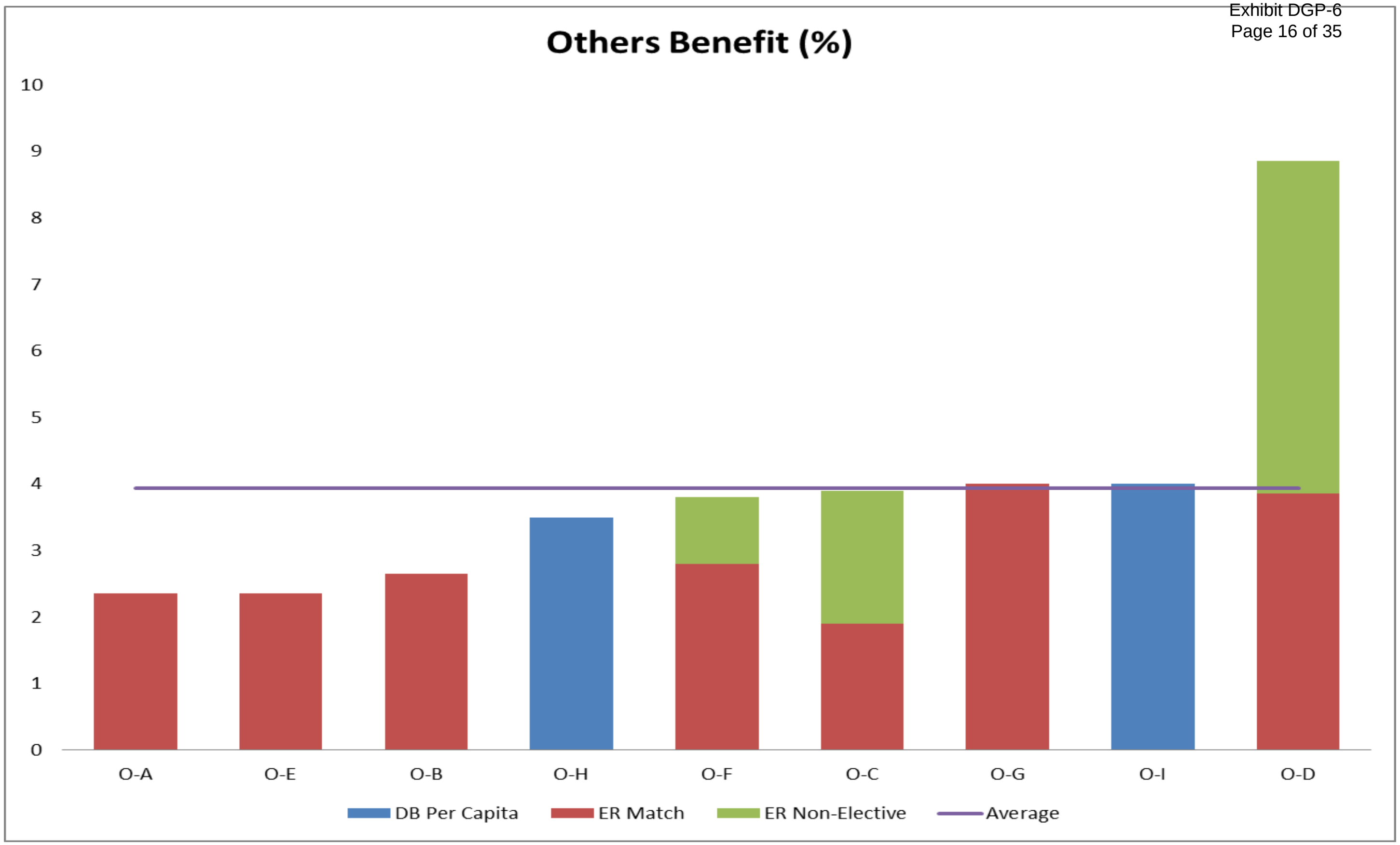
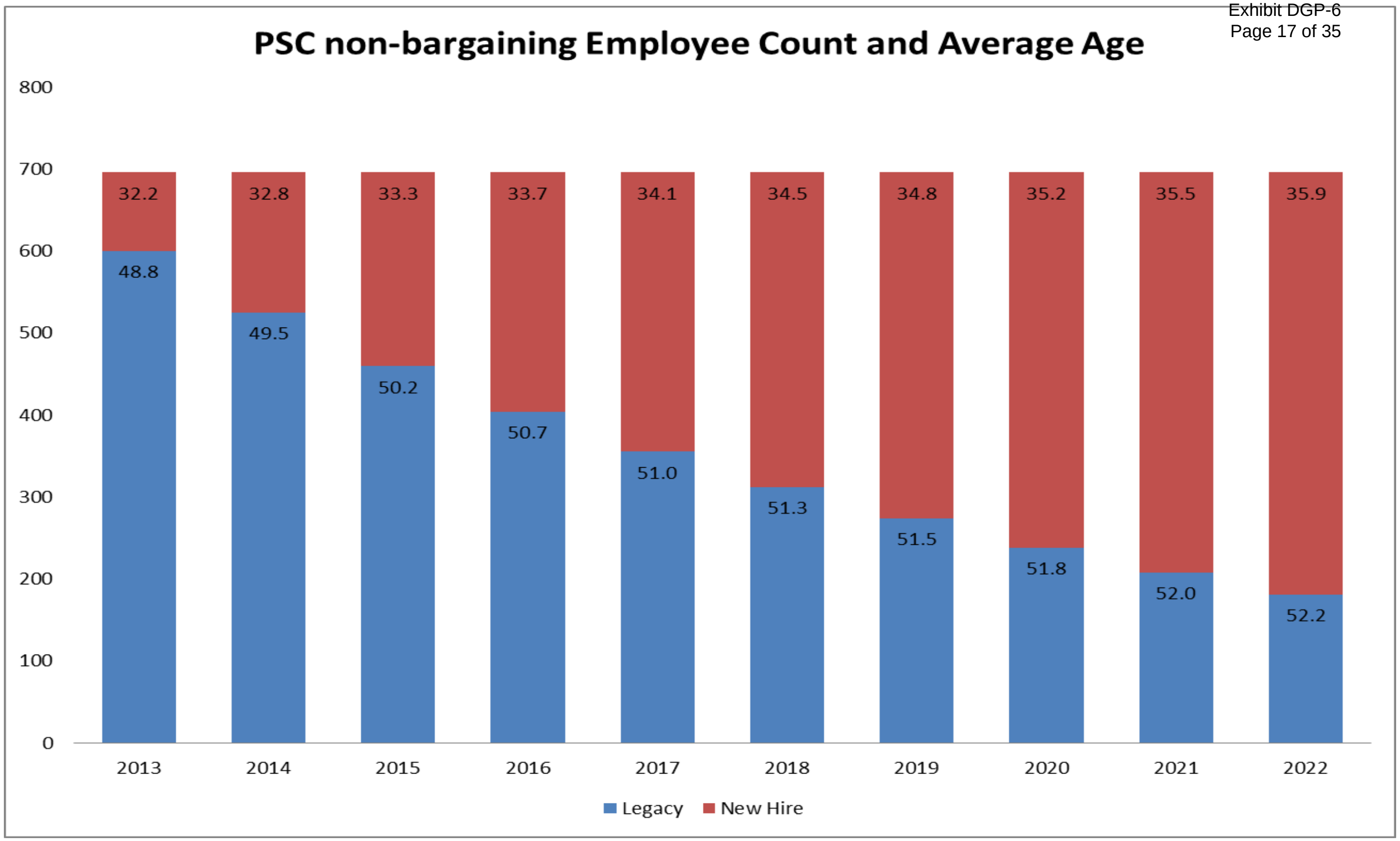


Chart 2-P: PSC Demographic Projection



MOODY'S ANALYTICS

Chart 2-X: Shared Service Group Demographic Projection

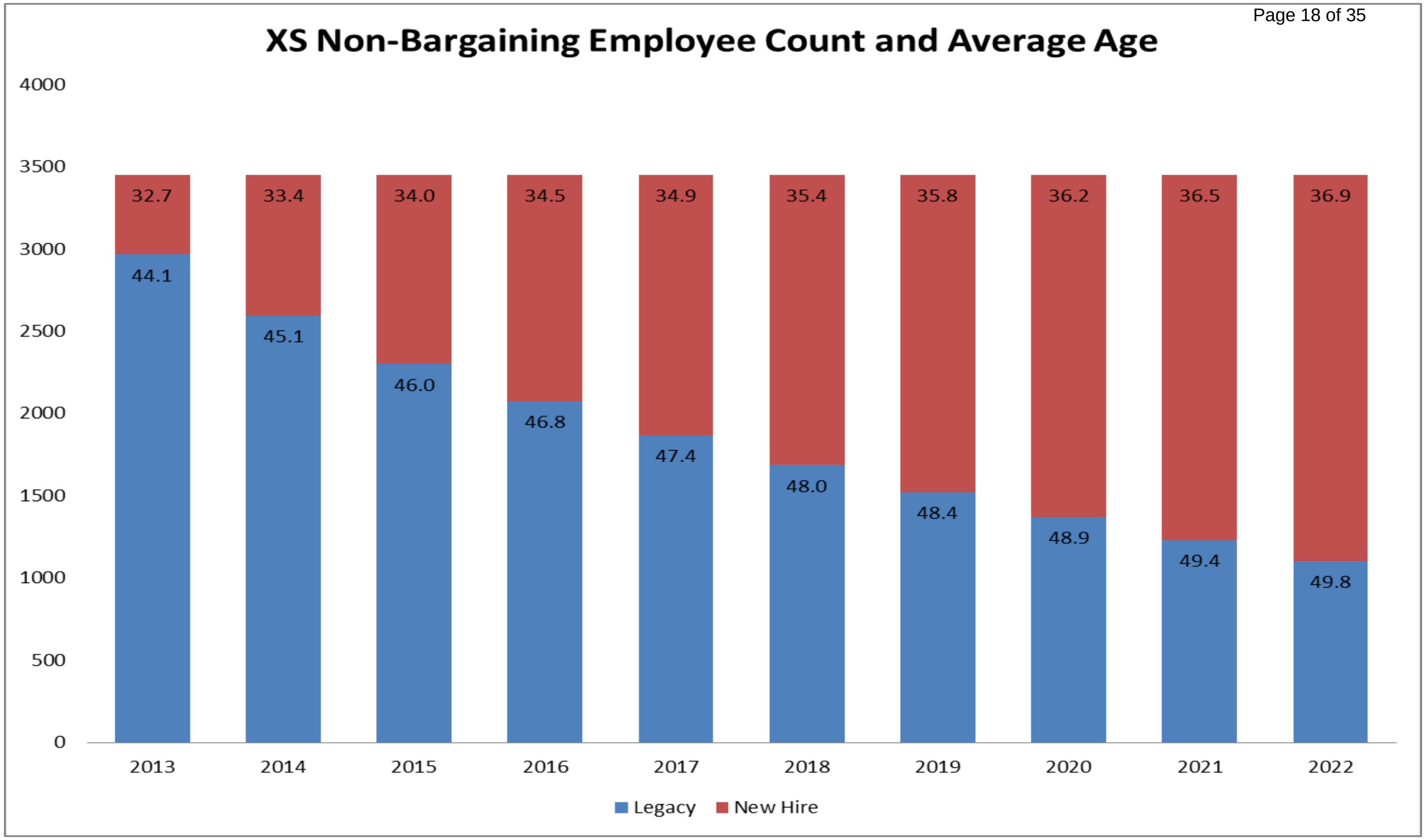


Chart 3-F: Retirement Wealth as a Multiple of Final Pay for Full Career Employee (excluding Social Security)

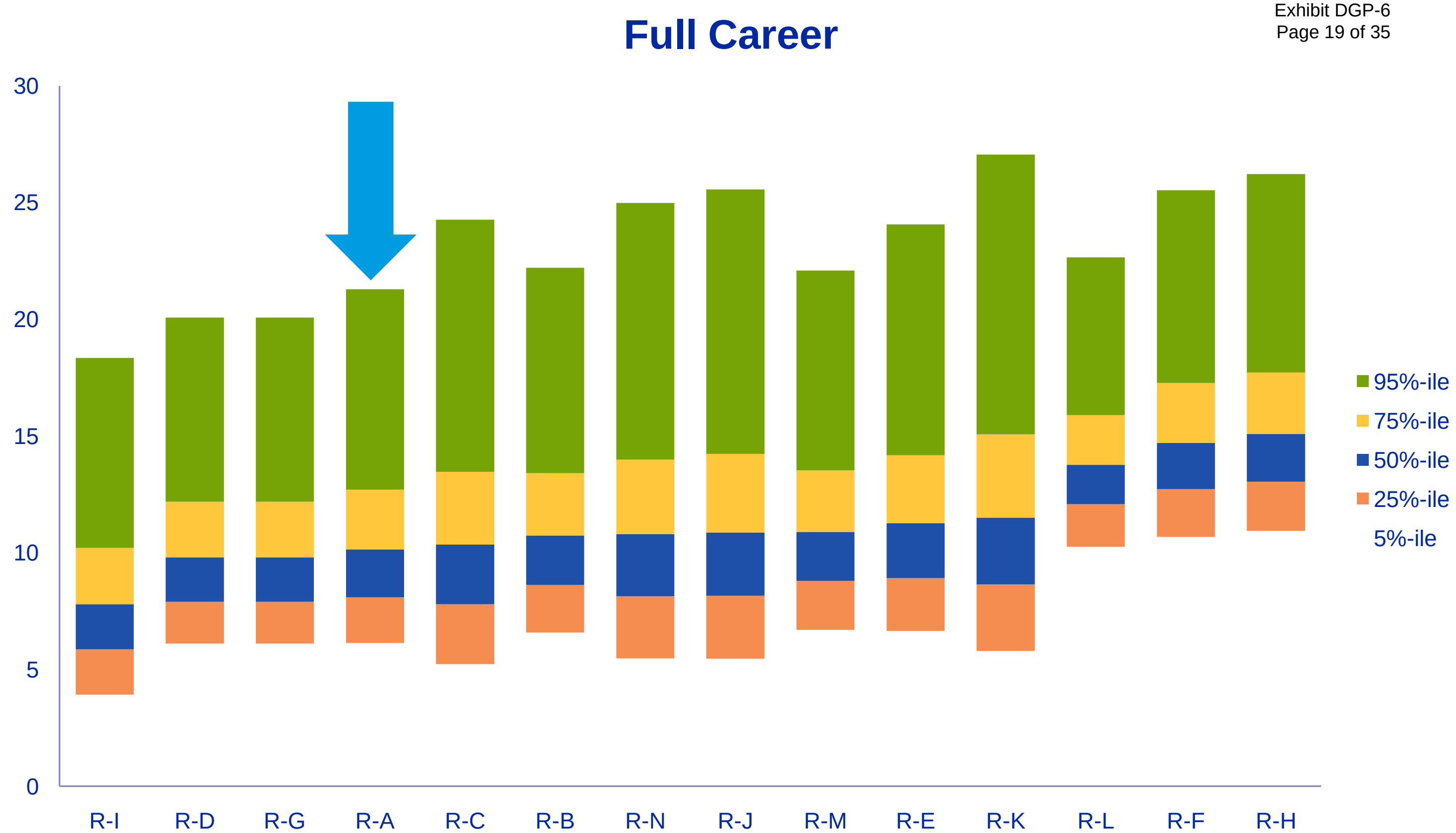


Chart 3-M: Retirement Wealth as a Multiple of Final Pay for Mid Career Hire (excluding Social Security)

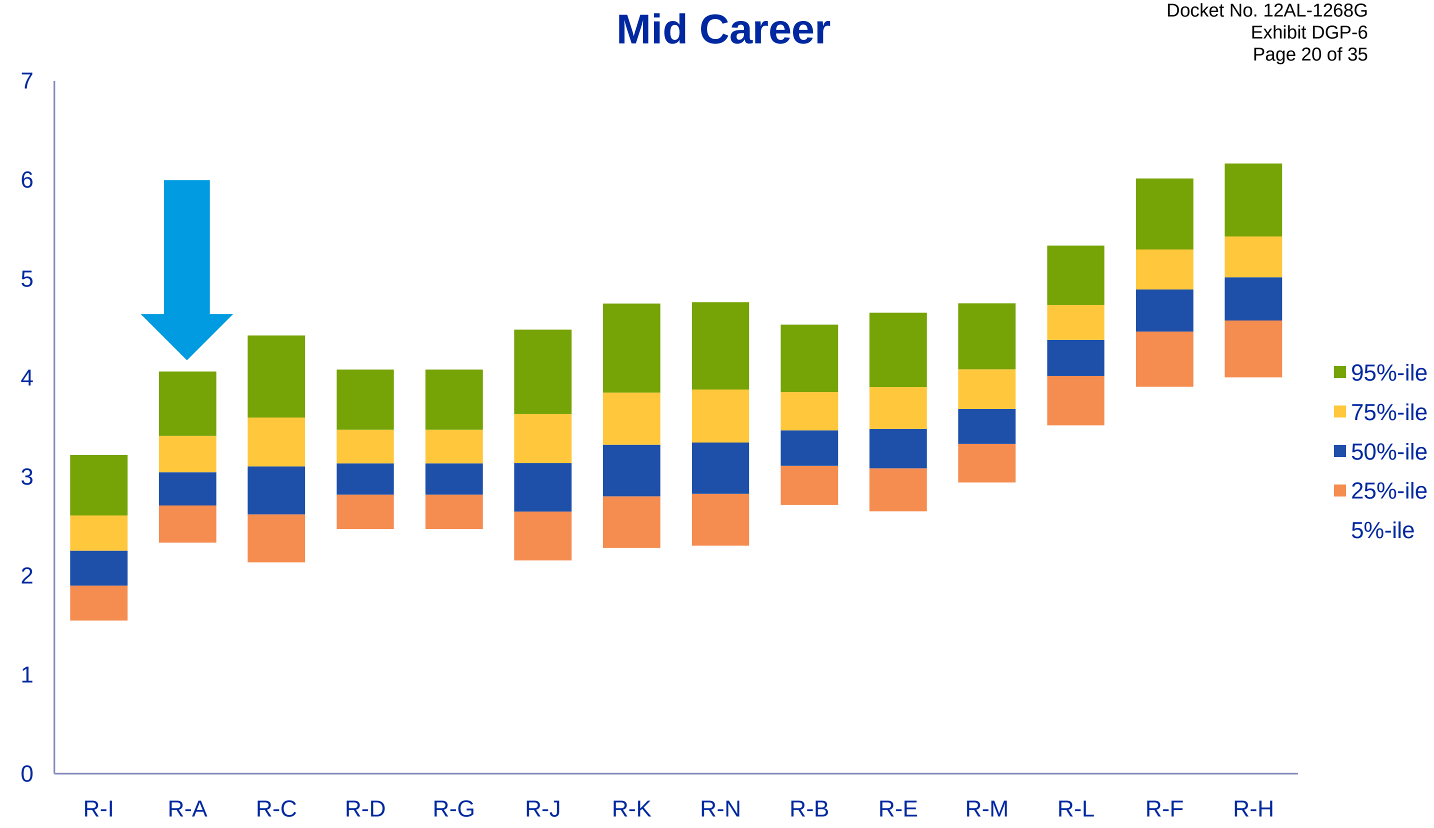


Chart 3-E: Retirement Wealth as a Multiple of Final Pay for Early Leaver (excluding Social Security)

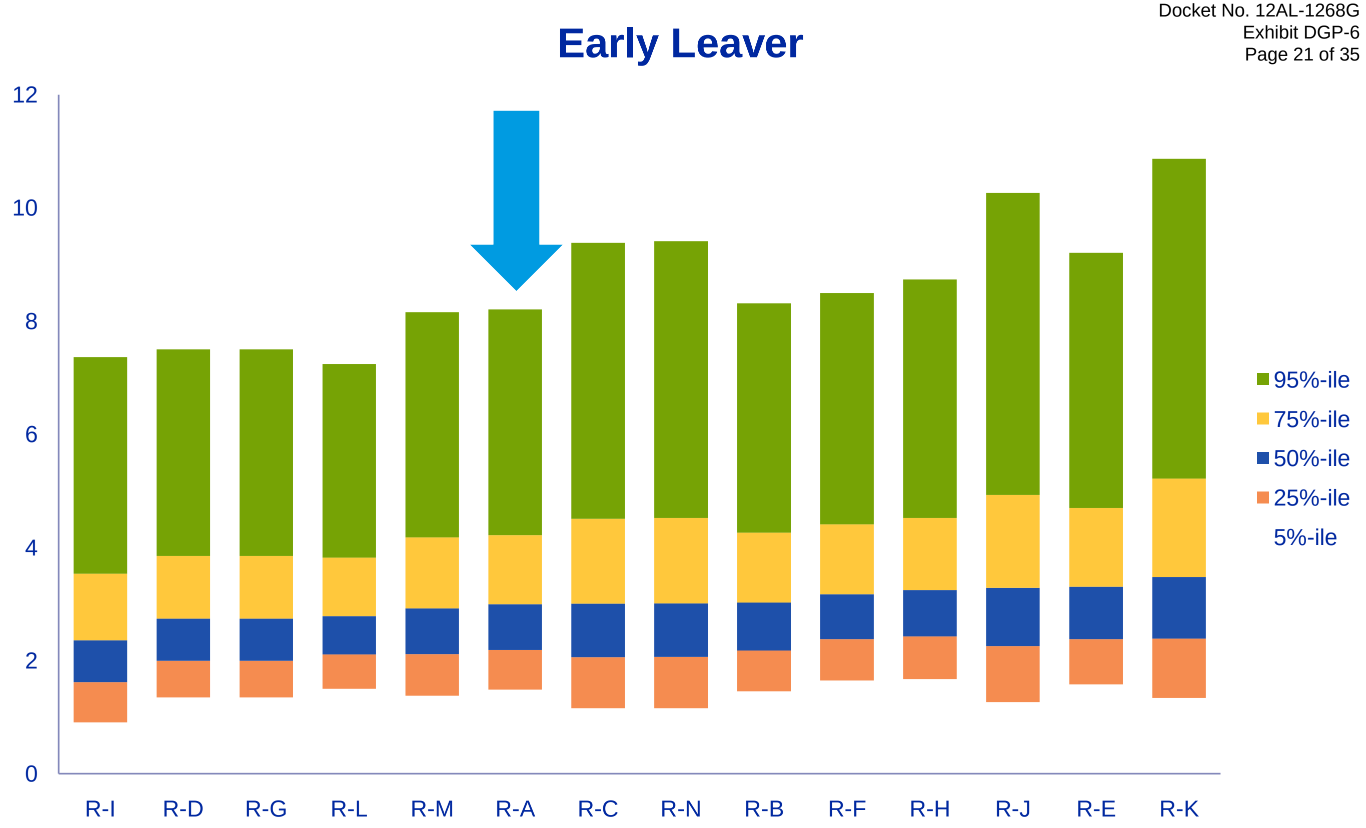


Table 1: Operational Cost Projections

Data Summary Actives Only

Barg	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000
NonB - Legacy	1,854	1,595	1,395	1,237	1,114	1,005	907	818	737	661
NonB - New	-	259	458	617	740	849	947	1,036	1,117	1,193
NonB - Total	1,854	1,854	1,854	1,854	1,854	1,854	1,854	1,854	1,854	1,854

Current Plan Projections

Per Capita Today $										
Barg	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000
NonB - Legacy	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000
NonB - New	5,300	5,300	5,300	5,300	5,300	5,300	5,300	5,300	5,300	5,300
Composite	15,000	14,348	13,846	13,447	13,138	12,862	12,616	12,393	12,189	11,997
Operational Costs	57.8	55.3	53.4	51.8	50.6	49.6	48.6	47.8	47.0	46.2

Table 1: Operational Cost Projections

Assuming Plan Wasn't Changed

Per Capita Today $										
Barg	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000
NonB - Legacy	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000
NonB - New	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000
Composite	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000
Operational Costs	57.8	57.8	57.8	57.8	57.8	57.8	57.8	57.8	57.8	57.8

Assuming All NonBargained Employees Covered Under New Plan Immediately

Per Capita Today $										
Barg	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000	15,000
NonB - Legacy	5,300	5,300	5,300	5,300	5,300	5,300	5,300	5,300	5,300	5,300
NonB - New	5,300	5,300	5,300	5,300	5,300	5,300	5,300	5,300	5,300	5,300
Composite	10,334	10,334	10,334	10,334	10,334	10,334	10,334	10,334	10,334	10,334
Operational Costs	39.8	39.8	39.8	39.8	39.8	39.8	39.8	39.8	39.8	39.8

Table 1: Operational Cost Projections

Impact of Plan Change ($Millions)	Over 3 years	Over 5 years	Over 10 years
Total Costs - Assuming Plan Was Not Changed	173.4	289.0	578.1
Total Costs with changes to New Hires Only	166.5	268.9	508.1
Savings	7.0	20.1	70.0
Total Costs with changes to All Non Bargained	119.5	199.1	398.3
Savings	53.9	89.9	179.8

Table 2: Prevalence Statistics

Defined Benefit Plan Prevalence - New Hire, Non-Bargained

	Number	No Plan / Frozen	Cash Balance	Pension Equity	Final Pay	Career Average	Money Purchase
Regulated	14	4	7	1	3	0	0
Non-regulated	8	4	2	0	1	0	1
Others	9	7	0	0	0	2	0

401(k) Plan - Maximum Matching and Non-Elective Contributions

	Number	< 3%	[3 - 4%)	[4 - 5%)	[5 - 6%)	[6 - 7%)	> 7%	Non-elective
Regulated	14	0	4	6	1	2	1	3
Non-regulated	8	0	3	1	1	3	0	3
Others	9	3	4	1	1	0	0	4

Table 3: Survey Participants

Regulated Utilities	Unregulated Utilities	Other Companies
Ameren Corporation	Atmos Energy Corporation	Alamo Group
Black Hills	California Water Service	Aspen Skiing
Consolidated Edison	CH Energy Group	Commercial Metals Company
Duke Energy	EQT Corporation	CPI Qualified Plan Consultant
Entergy	MDU Resources Group	Journal Communications
Madison Gas & Electric	NorthWestern Corporation	Kaydon Corporation
Northeast Utilities	Piedmont Natural Gas	Media News Group
NV Energy	Questar Corporation	NCH Corporation
OGE Energy		Strattec Security
Pepco Holdings		
Pinnacle West		
PNM Resources		
Public Service Co		
The Southern Company		

Table 4: New Hire Plan Summaries

Code	R-A	R-B	R-C	R-D
Defined Benefit Plan			Frozen to New Entrants	
Plan Type	Cash Balance	Cash Balance	N/A	Cash Balance
Normal Ret Age	65,1	65,5	N/A	65
Normal Retirement Benefit	Pay credit = 5%; interest credit = 30 year treasury rate from November of prior year	Pay Credit: Age + Service < 40 = 4%; 40 - 49 = 5%; 50 - 59 = 6%; 60 - 69 = 7%; 70 - 79 = 8%; more than 80 = 11%. Interest credit = 30 year Treasury Rate subject to 4.5% min and 10% max	N/A	Pay Credit based on Age + Svc Points with SSWB breakpoint: up to 35 points = 4/4, 35 - 49 = 5/4, 50 - 64 = 6/4, 65+ = 7/4. Interest credit applied quarterly; equals 1/4 of IRS applicable rate (min 0.75%, max 2.25%)
Pensionable Earnings	Base + bonus	Base	N/A	Base plus bonus (limited to 25% of base)
Other benefits	N/A	Pay credits continue during disability	N/A	N/A
Vesting Schedule	3 year	3 year	N/A	5 year
Defined Contribution Plan				
Matching Formula	50% employer match for first 8% of deferrals (match in ER stock fund)	75% employer match for first 6% of deferrals	100% match up to 6% deferral	50% match up to 6% deferral
Auto-enrollment features	4% automatic upon hire; 1% annual escalation until 10% deferral rate is reached	3% automatic upon hire	Auto enroll at 6%; will escalate 1% per year up to 10% (maybe more)	None
Vesting	Immediate	Immediate	5 year graded	3 years
Profit Sharing / Non-elective	None	None	Nonelective - age and years of service: < 34 : 1.5%; 35 - 44: 2%; 45 - 54: 2.5%; 55 - 64: 3%; 65 - 74: 3.5%; >75 : 4%	None

Table 4: New Hire Plan Summaries

Code	R-E	R-F	R-G	R-H
Defined Benefit Plan				
Plan Type	Cash Balance	Final Pay	Cash Balance	Final Pay
Normal Ret Age	65	65	65	65,5
Normal Retirement Benefit	Pay Credit based on Age + Svc Points. Less than 55 points = 4%; 55 - 59 = 5%; 60 - 64 = 6%; 65 - 69 = 7%; 70 + = 8%. Interest Credit based on 30 year Treasury from prior year, subject to a minimum crediting rate of 5.27%	1.25% of Final Average 3 times Years of Service	Pay Credit based on Age + Svc Points with SSWB breakpoint: up to 35 points = 4/4, 35 - 49 = 5/4, 50 - 64 = 6/4, 65+ = 7/4. Interest credit applied quarterly; equals 1/4 of IRS applicable rate (min 1%, max 2.25%)	1.3% of Final Average 5 times Years of Service
Pensionable Earnings	Total Pay	Base Pay	Total Pay	Base Pay
Other benefits	N/A	Subsidized early - 0.3% / month reduction until 50,10	N/A	Unreduced at 62,20; 3% reductions from 62 to 55,10
Vesting Schedule	5 year	5 year	3 year	5 year
Defined Contribution Plan				
Matching Formula	100% match up to 6% deferral	85% match up to 6% deferral	50% match up to 6% deferral	100% match up to 3% deferral; 50% match on next 5% of deferral
Auto-enrollment features	Yes	None	Auto-enrollment upon hire; no escalation	Auto enroll at 3%; 1% yearly escalation until 6%
Vesting	Immediate	Immediate	Immediate	Immediate
Profit Sharing / Non-elective	None	None	None	None

Table 4: New Hire Plan Summaries

Code	R-I	R-J	R-K	R-L
Defined Benefit Plan		None	None	
Plan Type	Pension Equity	N/A	N/A	Final Pay
Normal Ret Age	65	N/A	N/A	65
Normal Retirement Benefit	1.5 times Final Average Monthly Earnings (10 year period) times Years of Service	N/A	N/A	[1.25% of Final Average 5 up to Covered Comp plus 1.5% Final Average 5 in excess of Covered Comp] times Years of Service up to 25, plus 1.35% of Final Average 5 times Years of Service > 35
Pensionable Earnings	Base + Bonus	N/A	N/A	Base + OT + Shift Differentials
Other benefits	N/A	N/A	N/A	Subsidized Early (2% ERF from 65 to 60; 3% ERF from 60 to 55)
Vesting Schedule	5 year cliff	N/A	N/A	5 year
Defined Contribution Plan				
Matching Formula	70% match up to 6% deferral	50% match up to 6% deferral	200% match up to 5% deferral	100% match up to 3% of deferral
Auto-enrollment features	Upon hire	Auto-enrollment at 4%; increases 1% annually thereafter	Auto-enrollment at 3%; increases 2% annually thereafter until 19% reached	Auto-enrollment upon hire; discretionary escalation
Vesting	Immediate	Immediate	3 year graded	Immediate
Profit Sharing / Non-elective	None	6%	None	None

Table 4: New Hire Plan Summaries

Code	R-M	R-N	U-A	U-B
Defined Benefit Plan		Frozen to New Entrants		
Plan Type	Cash Balance	N/A	Money Purchase	Final Pay
Normal Ret Age	65	N/A	65	65
Normal Retirement Benefit	Pay Credits are age based: <30 = 3%, 30 - 34 = 4%, 35 - 39 = 4%, 40 - 44 = 5%, 45 - 49 = 6%, 50 - 54 = 7%, 55+ = 8%. Additional pay credit of 3% for excess earnings above SSWB. Enhancement credit of $500. Interest credit = 1 year Treasury + 1% or 5% if greater	N/A	Account balance based on employer contributions of 4% of Earnings plus 4% of Excess Earnings (over SSWB)	1.5% of Final Average 3 times Years of Service (max 35)
Pensionable Earnings	Total Pay	N/A	Total Pay	Total Pay
Other benefits	N/A	N/A	N/A	N/A
Vesting Schedule	3 year	N/A	3 year	5 year
Defined Contribution Plan				
Matching Formula	100% match up to first 3% of deferral; 50% match on next 3% of deferral	75% match up to 6% of deferral	100% match up to 5% deferral	75% match up to 8% of deferral
Auto-enrollment features	Auto-enrollment upon hire; annual escalation	Auto-enrollment upon hire	2% automatic upon hire; 1% escalation per year until 5% deferral rate is reached	Auto-enrollment at 3% upon hire
Vesting	Immediate	Immediate	6 months	Immediate
Profit Sharing / Non-elective	None	Age weighted - e.g., an additional 5% at age 45, an additional 6% at age 50	None	None

Table 4: New Hire Plan Summaries

Code	U-C	U-D	U-E	U-F
Defined Benefit Plan		Frozen to new entrants	None	Frozen to new entrants
Plan Type	Cash Balance	N/A	N/A	N/A
Normal Ret Age	65	N/A	N/A	N/A
Normal Retirement Benefit	Pay Credit = 3% / 6% at SSWB; Interest Credit based on 30 Year Treasury	N/A	N/A	N/A
Pensionable Earnings	Total Pay	N/A	N/A	N/A
Other benefits	N/A	N/A	N/A	N/A
Vesting Schedule	3 year	N/A	N/A	N/A
Defined Contribution Plan				
Matching Formula	50% match up to 6% of deferral	50% match up to 6% of deferral	100% match up to 6% of deferral	50% match up to 8% of deferral
Auto-enrollment features	Auto-enrollment at hire and annually	Auto-enrollment at hire and annually until 15%	Auto-enrollment at hire of 6%	Auto-enrollment at hire
Vesting	Immediate	Immediate	1 year	Immediate
Profit Sharing / Non-elective	None	Approximately 5%	None	3% additional non-elective for new hires

Table 4: New Hire Plan Summaries

Code	U-G	U-H	O-A	O-B
Defined Benefit Plan	None		None	None
Plan Type	N/A	Cash Balance	N/A	N/A
Normal Ret Age	N/A	65	N/A	N/A
Normal Retirement Benefit	N/A	Pay Credit based on Age + Svc Points with SSWB breakpoint: up to 35 points = 2.35/2.35, 35 - 49 = 3.25/3.25, 50 - 64 = 4.5/4.5, 65 -79 = 6.25/5, 80 - 94 = 8.5/5, 95+ = 10.5/5. Interest credit equals 30 Year Treasury (min 4.69% max 7.0%)	N/A	N/A
Pensionable Earnings	N/A	Total Pay	N/A	N/A
Other benefits	N/A	N/A	N/A	N/A
Vesting Schedule	N/A	3 year	N/A	N/A
Defined Contribution Plan				
Matching Formula	50% match up to 6% deferral	100% match up to 6% deferral	50% match up to 6% of deferral	50% match up to 7% deferral
Auto-enrollment features	None	Auto-enrollment at hire and annual escalation	Auto-enrollment at hire of 3%	Auto enroll at 2%; 1% escalation thereafter
Vesting	3 year graded	3 year	5 year graded	1 year
Profit Sharing / Non-elective	None	4%	None	None

Table 4: New Hire Plan Summaries

Code	O-C	O-D	O-E	O-F
Defined Benefit Plan	None	None	None	None
Plan Type	N/A	N/A	N/A	N/A
Normal Ret Age	N/A	N/A	N/A	N/A
Normal Retirement Benefit	N/A	N/A	N/A	N/A
Pensionable Earnings	N/A	N/A	N/A	N/A
Other benefits	N/A	N/A	N/A	N/A
Vesting Schedule	N/A	N/A	N/A	N/A
Defined Contribution Plan				
Matching Formula	100% match up to 2% deferral	100% match up to 3% deferral; 50% match on next 3% of deferral	50% match up to 6% deferral	100% match up to 3% deferral
Auto-enrollment features	None	Auto-enrollment upon hire; annual escalation up to 8%	None	None
Vesting	5 years	Immediate	3 year graded	3 year
Profit Sharing / Non-elective	2%	Average of 5%	None	100% match up to $750

Table 4: New Hire Plan Summaries

Code	O-G	O-H	O-I
Defined Benefit Plan	None		
Plan Type	N/A	Career Average	Career Pay
Normal Ret Age	N/A	65	65
Normal Retirement Benefit	N/A	1% of Career Average times Years of Service (max 30)	2% of annual pay through age 50 plus 2.5% of annual pay after age 50
Pensionable Earnings	N/A	Total Pay	Base pay
Other benefits	N/A	Partially subsidized early (50% ERF at age 55,10)	N/A
Vesting Schedule	N/A	5 year	5 year
Defined Contribution Plan			
Matching Formula	100% match up to 5% deferral	Match suspended in 2008	None
Auto-enrollment features	None	N/A	None
Vesting	Immediate	N/A	5 year graded
Profit Sharing / Non-elective	None	N/A	3%