

Before the North Dakota Public Service Commission
State of North Dakota

In the Matter of the Application of Otter Tail Power Company
For Authority to Increase Rates for Electric Utility
Service in North Dakota

Case No. PU-17-

Exhibit____

**BUDGET PROCESS,
OPERATIONS AND MAINTENANCE EXPENSES,
PENSION AND POST EMPLOYMENT EXPENSES**

Direct Testimony and Schedules of

CHRISTINE L. PETERSEN

November 2, 2017

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Schedule 1 – Petersen Qualifications and Responsibilities

Schedule 2 – Schedule of Operations and Maintenance Expense

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1 **I. INTRODUCTION AND QUALIFICATIONS**

2 Q. PLEASE STATE YOUR NAME AND OCCUPATION.

3 A. My name is Christine L. Petersen. I am employed by Otter Tail Power Company (OTP)
4 as Financial/Rates Analyst, Business Planning/Regulatory Accounting Department.

6 Q. PLEASE SUMMARIZE YOUR QUALIFICATIONS AND EXERIENCE.

7 A. I began my current position as Financial/Rates Analyst, Business Planning/Regulatory
8 Accounting in May 2010. My primary responsibilities are producing the jurisdictional
9 cost of service studies for the three state jurisdictions in which OTP provides service
10 (Minnesota, North Dakota, and South Dakota) and providing other regulatory and
11 financial analysis. In addition, I provide financial analysis of OTP's Operations and
12 Maintenance (O&M) expenses.

13 I have been employed by OTP since May 2010. Prior to that, I was a
14 Governmental Auditor at a CPA firm in Fergus Falls. A summary of my qualifications,
15 experience, duties and responsibilities is included as Exhibit___(CLP-1), Schedule 1.

16 **II. PURPOSE AND OVERVIEW OF DIRECT TESTIMONY**

17 Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?

18 A. My Direct Testimony supports OTP's financial schedules and the O&M expenses that are
19 included in OTP's revenue requirement and deficiency for the 2018 Test Year. OTP
20 witness Mr. Tyler A. Akerman presents the OTP's overall revenue requirement and
21 revenue deficiency for the 2018 Test Year.

23 Q. PLEASE PROVIDE A BRIEF OVERVIEW OF YOUR DIRECT TESTIMONY.

24 A. I explain the O&M portion of OTP's expense budget (O&M Budget), including the
25 process used to develop the O&M Budget. The O&M Budget serves as the basis for the
26 development of the 2018 Test Year Income Statement. I also provide information
27 pertaining to pension and benefit expenses.

1 Q. HOW IS YOUR DIRECT TESTIMONY ORGANIZED?

2 A. Section III describes the process used to establish OTP's 2018 O&M Budget and the uses
3 made of the O&M Budget. Section IV presents the schedule of O&M expenses included
4 in the 2018 Test Year and describes some significant elements of the O&M expenses for
5 the 2018 Test Year, including pension expense and its impact on the 2018 Test Year
6 revenue requirement. Section V presents my conclusions.

7

8 Q. DID YOU USE ANY LABELING CONVENTIONS IN YOUR DIRECT TESTIMONY?

9 A. Yes. In the great majority of my Direct Testimony, I am presenting the discussion on an
10 OTP Total Company basis. When doing so, I have not used any further description or
11 parenthetical notation. There are certain power plant and transmission projects where
12 OTP is only a part owner. In those circumstances, I included each of the following: the
13 total project costs, labeled as (Total Plant or Total Project), the OTP ownership allocation
14 of the project amounts, labeled as (OTP Total), and the North Dakota Jurisdictional share,
15 labeled as (OTP ND). There may also be instances with project-related amounts where
16 an estimate must be made of OTP's jurisdictional share of such costs, which are labeled
17 as (OTP ND EST).

18 **III. O&M BUDGET**

19 Q. WHAT IS THE PURPOSE OF THIS SECTION OF YOUR DIRECT TESTIMONY?

20 A. In this section of my Direct Testimony, I will provide an overview of the process used to
21 develop OTP's O&M Budget. I will identify the participants in the O&M Budget, and
22 describe the processes used by each. I will also describe how the O&M Budget is used.

23

24 Q. DOES OTP'S 2018 O&M BUDGET PROVIDE A REASONABLE BASIS FOR THE
25 2018 TEST YEAR?

26 A. Yes. OTP used appropriate processes to develop its 2018 O&M Budget, and the 2018
27 O&M Budget reflects reasonable levels of increased O&M expenses.

1 **A. O&M Budget Process**

2 Q. PLEASE IDENTIFY THE PRIMARY PARTICIPANTS IN OTP’S O&M BUDGETING
3 PROCESS.

4 A. Several groups within OTP have significant roles in the O&M Budgeting process:
5 Business Areas within OTP, which include Regulatory Affairs, Asset Management,
6 Customer Service, Energy Supply, Finance, Human Resources, Planning and Strategy,
7 and the Public Relations and Information Technology Departments. The Vice Presidents
8 of the Business Areas and Department Managers within the Business Areas also have
9 significant roles.

10 The Business Planning Department (which is part of the Finance Area) has a
11 central role in establishing the O&M Budgets. The Business Planning Department’s
12 responsibilities include establishing targets, preliminary estimates, and criteria and
13 providing coordination, evaluation, and oversight of O&M Budgets.

14 In addition, the Chief Financial Officer (CFO) and Chief Executive Officer (CEO)
15 of OTP have significant roles. The roles of the CFO and CEO include conferring with
16 Business Area Vice Presidents as budgets are being refined and reviewing the O&M
17 Budget as it is being developed by Business Planning. The OTP Board of Directors and
18 the Otter Tail Corporation Board of Directors provide final approval of the OTP O&M
19 Budget.

20
21 Q. PLEASE PROVIDE AN OVERVIEW OF THE BASIS AND TIMELINE FOR
22 DEVELOPING THE OTP O&M BUDGET.

23 A. The OTP O&M Budget is developed primarily in the second quarter of the year before
24 the budget year. Accordingly, the 2018 O&M Budget was developed primarily in the
25 second quarter of 2017. For the 2018 O&M Budget, the starting point was the 2017
26 Forecast, with adjustments being made to reflect known changes for 2018 as the 2018
27 Budget was being developed.

28 The process begins in the second quarter with the development of preliminary
29 estimates and targets by the Business Planning Department. The Business Areas review

1 and propose modifications to the preliminary estimates and targets in the second and third
2 quarters. This process was used for the 2018 O&M Budget.

3 An updated budget was prepared by Business Planning in June 2017, which was
4 also subject to further review by the Business Areas.

5 After review by the Business Areas, the 2018 O&M Budget will be presented to,
6 and approved by, the OTP Board of Directors and thereafter by the Otter Tail
7 Corporation Board of Directors early in the fourth quarter of 2017.

8
9 Q. WHAT SYSTEMS DOES OTP USE FOR O&M BUDGETING?

10 A. OTP uses a software package called Utilities International (UI) in developing its budgets.
11 UI is used by a number of utilities for budgeting, forecasting, financial reporting, and cost
12 of service studies. OTP transitioned to UI in 2013. The O&M Budget is prepared using
13 only UI.

14
15 Q. WHAT ARE THE PRIMARY COMPONENTS OF THE O&M BUDGET?

16 A. O&M costs are made up of two primary components: Labor and Non-Labor costs.
17

18 Q. HOW WERE BUDGETED LABOR COSTS DEVELOPED?

19 A. Budgeted Labor costs are developed based on individual employees within each
20 Department within each Business Area, and are then cumulated at the Business Area
21 level. The process begins with target Full-Time Equivalent (FTE) employee projections
22 provided to the Department Managers by the Business Planning Department in the
23 second quarter of the year prior to the budget year. For the 2018 O&M Budget, these
24 targets were based primarily on 2016 employee levels.

25 A composite labor rate is determined for each Business Area based on total
26 employee salaries for each Department within the Business Area. An inflationary rate is
27 also determined based on existing contracts and estimated cost increases and applied to
28 bring the basic Labor costs to the Budget Year level. Overtime projections are also made
29 and included. A labor loading rate is also applied to all basic labor costs. The labor

1 loading rate reflects lost time, payroll taxes, and benefit costs. This process was used for
2 the 2018 O&M Budget.

3
4 Q. HOW WAS THE LABOR RATE DETERMINED?

5 A. The Human Resources Area works with the Vice Presidents of the Business Areas as well
6 as the OTP President and Chief Financial Officer (CFO) to develop the estimate of the
7 overall annual labor rate to expect for all non-union employees for the Budget Year. The
8 Labor rate for union employees is based on contracts between OTP and the respective
9 unions, including any increases that will become effective in 2018. Overall labor costs
10 are finalized by the Human Resources Area.

11
12 Q. HOW ARE BUDGETED NON-LABOR COSTS DEVELOPED?

13 A. The Non-Labor O&M Budget is developed by the Business Planning Department. For
14 the 2018 budget, the Department began with the 2017 forecast and it requested
15 adjustments from Department Managers. These adjustments were made to reflect
16 changes that were known for the 2018 Budget Year, either adding or reducing costs for
17 known changes and expected major events, such as generating plant outages. The
18 Budgeting department also established a 3 percent limitation for any proposed increases,
19 with special review was required prior to approval of any increases beyond that
20 limitation.

21 If the Department Managers determined the budget would increase by an amount
22 that would exceed the 3 percent imitation, the Business Area Vice President was required
23 to review and verify the budget to determine if the added amount was appropriate.
24 Efforts were made to balance amounts that may exceed a Business Area's target by
25 decreases in other Business Areas within the Department.

26 For any amounts over the 3 percent limitation approved by the Business Area
27 Vice President, final approval was also required from the OTP President and CFO.
28 Approval of the overall O&M Budget (which includes Labor and Non-Labor O&M) by
29 the OTP Board of Directors and Otter Tail Corporation Board is also required.
30

1 Q. HAS OTP PROVIDED FURTHER INFORMATION ON THE DEVELOPMENT OF
2 LABOR AND NON-LABOR COSTS IN CONNECTION WITH THIS APPLICATION?

3 A. Yes. Further information about the Labor and Non-Labor components of the O&M
4 Budget are contained in Volume 5, Budget Documentation.

5 **B. O&M Budget Results**

6 Q. HAVE YOU COMPARED OTP'S ACTUAL O&M RESULTS TO OTP'S O&M
7 BUDGETS?

8 A. Yes. I have reviewed and compared OTP's actual O&M results by FERC account to
9 OTP's O&M Budgets by FERC account for the years 2012 through 2016.

10

11 Q. PLEASE SUMMARIZE THE RESULTS OF YOUR COMPARISON.

12 A. OTP's actual O&M expenses have been, on average, within 1.49 percent of budget for
13 the three-year period 2014 through 2016 and within 1.56 percent of budget for the five-
14 year period 2012 through 2016. Vol. 5, Budget Documentation, contains additional
15 information pertaining to comparisons of OTP's O&M Budgets to actual results.

16

17 Q. HAVE YOU ALSO COMPARED O&M BUDGETS TO O&M ACTUAL EXPENSES
18 FOR 2015 AND 2016?

19 A. Yes. In 2015, OTP's actual O&M expenses were 3.62 percent below OTP's 2015 Budget
20 O&M expense primarily because the major planned boiler project for Big Stone
21 developed into a much larger project than was anticipated. The boiler work was
22 originally considered to be a routine O&M project, which led to including the costs in the
23 O&M budget. As the project developed in 2015, it was determined that the changes that
24 needed to be made to the Big Stone boiler would prolong its life. As a result, the decision
25 was made that the associated costs should be capitalized. In addition, the Coyote, Hoot
26 Lake and Solway plants running at half capacity through most of 2015, minimizing
27 normal O&M expenses. When adjustments are made for the effects of these events,
28 OTP's 2015 actual O&M expenses are within 1.31 percent of the 2015 O&M Budget.

29 In 2016, OTP's actual O&M expense was approximately 4.82 percent below
30 OTP's 2016 Budget O&M expense, largely because of the combined effects of: (1) Hoot

1 Lake and Solway plants were offline due to reduced dispatch demand for energy by the
2 Midcontinent Independent System Operator (MISO); (2) changes in planned outage
3 levels at Coyote and Big Stone plants; and (3) an increase in construction labor dollars
4 therefore reducing O&M labor dollars. When adjustments are made for the effects of
5 these factors, OTP's 2016 actual O&M expenses are within 1.48 percent of the 2016
6 O&M Budget.

7
8 Q. ARE THERE SOME EXPENSE COMPONENTS WITHIN THE 2018 BUDGET THAT
9 REFLECT SIGNIFICANT CHANGES FROM 2017 BUDGET?

10 A. Yes. The 2018 O&M Budget reflects expense increases of: (1) approximately
11 \$2,500,000 of expenses relating to a planned periodic maintenance outage at Big Stone;
12 (2) approximately \$1,000,000 in additional charges from MISO; (3) approximately
13 \$2,800,000 in pension related charges resulting from Accounting Standards Codification
14 715 (ASC 715); and (4) approximately \$3,200,000 in expenses relating to pensions and
15 other retirement benefits resulting from decreases in the applicable discount rates and the
16 estimated Earned Return On Assets (EROA) for 2018. The remainder of increases in
17 OTP's 2018 O&M Budget were approximately 3.1 percent above OTP's 2017 O&M
18 Budget.

19 Mr. Akerman will explain the adjustment made to normalize maintenance
20 expenses for 2018. I will discuss the pension expenses resulting from ASC 715 and the
21 pension and other benefit expenses resulting from decreases in applicable discount rates
22 and the EROA.

23
24 Q. HOW HAVE OTP'S ACTUAL O&M EXPENSES CHANGED BETWEEN 2012 AND
25 2016?

26 A. OTP's actual O&M expenses increased from \$104 million in 2012 to \$121 million in
27 2016. This represents a \$17 million or 16 percent increase over 5 years, which is a 2.7
28 percent average annual increase. This level of historic actual O&M expense increase is
29 consistent with the approach that we have taken to OTP's O&M budget for 2018 and
30 prior years.

1 Q. WHAT CONCLUSIONS DO YOU DRAW FROM THESE FACTS?

2 A. The OTP 2018 O&M Budget that is reflected in OTP's proposed 2018 Test Year is
3 reasonable and reliable. The basic assumptions underlying OTPs' O&M Budget are
4 reasonable and allow the Commission to test the appropriateness of OTP's 2018 Test
5 Year. OTP's accounting treatment of anticipated 2018 O&M Expenses and transactions
6 is the same as has been used in prior years. OTP's 2018 O&M budget provide an
7 accurate and reliable basis for setting rates.

8 **IV. O&M EXPENSES**

9 Q. WHAT IS THE PURPOSE OF THIS SECTION OF YOUR DIRECT TESTIMONY?

10 A. In this section of my Direct Testimony, I will briefly describe the components in the
11 Schedule of OTP's O&M expenses for the 2018 Test Year, including unadjusted and
12 adjusted amounts. Mr. Akerman will discuss some of the more significant elements of
13 O&M expenses for the 2018 Test Year in his Direct Testimony.

14 **A. Schedule of O&M Expenses**

15 Q. DOES EXHIBIT__(CLP-1), SCHEDULE 2 INCLUDE ALL O&M EXPENSES?

16 A. Yes. Exhibit__(CLP-1), Schedule 2, the Schedule of O&M Expenses, includes all
17 O&M expenses, whether they are specifically discussed by me or by other OTP
18 witnesses. In this subsection of my Direct Testimony I will identify each category of
19 O&M Expense and briefly list the types of expenses included in each category.

20 **1. Production Expenses**

21 Q. WHAT IS THE AMOUNT OF PRODUCTION EXPENSE INCLUDED IN
22 EXHIBIT__(CLP-1), SCHEDULE 2?

23 A. Exhibit__(CLP-1), Schedule 2 shows that OTP's North Dakota Jurisdictional
24 Production Expense is \$60.1 million before adjustments and \$59.8 million after
25 adjustments. Mr. Akerman will explain the difference between the unadjusted and
26 adjusted amounts in his Direct Testimony.

27

1 Q. WHAT IS INCLUDED IN PRODUCTION EXPENSE?

2 A. The most significant Production Expense is Fuel and Purchased Power. Production
3 Expense also includes maintenance costs of OTP's generation plants. The Direct
4 Testimony of OTP witness Mr. Stuart D. Tommerdahl discusses Fuel and Purchased
5 Power Expense.

6 **2. Transmission Expenses**

7 Q. WHAT IS THE AMOUNT OF TRANSMISSION EXPENSE INCLUDED IN
8 EXHIBIT__(CLP-1), SCHEDULE 2?

9 A. Exhibit__(CLP-1), Schedule 2 shows that OTP's North Dakota Jurisdictional
10 Transmission Expense is \$13.5 million before and after adjustments.

11

12 Q. WHAT IS INCLUDED IN TRANSMISSION EXPENSE?

13 A. Transmission expense includes: Load dispatching, Substation expense, Maintenance of
14 transmission lines and substations, Transmission of electricity by others, Rents for
15 transmission property, Engineering, Computer Hardware and Software for operation of
16 the transmission system, and Transmission Market Costs.

17 **3. Distribution Expenses**

18 Q. WHAT IS THE AMOUNT OF DISTRIBUTION EXPENSE INCLUDED IN
19 EXHIBIT__(CLP-1), SCHEDULE 2?

20 A. Exhibit__(CLP-1), Schedule 2 shows that OTP's North Dakota Jurisdictional
21 Distribution Expense is \$7.7 million before adjustments and after adjustments.

22

23 Q. WHAT IS INCLUDED IN DISTRIBUTION EXPENSE?

24 A. Distribution Expense includes: expenses for operation and maintenance of the
25 distribution system, including substations, wires, transformers, meters and lighting.

1 **4. Customer Accounting Expenses**

2 Q. WHAT IS THE AMOUNT OF CUSTOMER ACCOUNTING EXPENSE INCLUDED
3 IN EXHIBIT___(CLP-1), SCHEDULE 2?

4 A. Exhibit___(CLP-1), Schedule 2 shows that OTP’s North Dakota Jurisdictional Customer
5 Accounting Expense is \$6.1 million before adjustments and after adjustments.

6 Q. WHAT IS INCLUDED IN CUSTOMER ACCOUNTING EXPENSE?

7 A. Customer Accounting Expense includes: Meter Reading, billing and maintenance of
8 customer records (customer information systems).

9 **5. Customer Service and Information Expenses**

10 Q. WHAT IS THE AMOUNT OF CUSTOMER SERVICE AND INFORMATION
11 EXPENSE INCLUDED IN EXHIBIT___(CLP-1), SCHEDULE 2?

12 A. Exhibit___(CLP-1), Schedule 2 shows that OTP’s North Dakota Jurisdictional Customer
13 Accounting Expense is \$1.4 million before adjustments and after adjustments.

14
15 Q. WHAT IS INCLUDED IN CUSTOMER SERVICE AND INFORMATION EXPENSE?

16 A. Customer Service and Information Expense includes: Customer assistance expenses.

17 **6. Sales Expense**

18 Q. WHAT IS THE AMOUNT OF SALES EXPENSE INCLUDED IN EXHIBIT___ (CLP-
19 1), SCHEDULE 2?

20 A. Exhibit___(CLP-1), Schedule 2 shows that OTP’s North Dakota Jurisdictional Sales
21 Expense is \$22,000 before adjustments and \$222,000 after adjustments. Mr. Akerman
22 will explain the difference between the unadjusted and adjusted amounts in his Direct
23 Testimony.

24
25 Q. WHAT IS INCLUDED IN SALES EXPENSE?

26 A. Sales Expense includes: Selling and Advertising Expenses as well as Economic
27 Development Costs.

1 **7. Administrative and General Expenses**

2 Q. WHAT IS THE AMOUNT OF ADMINISTRATIVE AND GENERAL EXPENSE
3 INCLUDED IN EXHIBIT___(CLP-1), SCHEDULE 2?

4 A. Exhibit___(CLP-1), Schedule 2 shows that OTP’s North Dakota Jurisdictional
5 Administrative and General Expense is \$20.1 million before adjustments and \$19.6
6 million after adjustments. Mr. Akerman will explain the difference between the
7 unadjusted and adjusted amounts in his Direct Testimony.

8
9 Q. WHAT IS INCLUDED IN ADMINISTRATIVE AND GENERAL EXPENSE?

10 A. Administrative and General Expense includes: Salaries, Office Supplies & Expenses,
11 Various Admin & General Expenses, Outside Services Employed, Property Insurance,
12 Injuries & Damage, Employee Pensions & Benefits, Regulatory Commission Expenses,
13 Miscellaneous General Expenses, Informational Advertising, Rents, and Building
14 Maintenance Expenses.

15 **8. Compensation and Employee Benefits**

16 Q. HAVE YOU REFLECTED IN O&M EXPENSES THE 2018 TEST YEAR WAGE AND
17 INCENTIVE COMPENSATION AND EMPLOYEE BENEFITS EXPENSES?

18 A. Yes. The wage and incentive compensation and employee benefits expenses that are
19 described by OTP witness Mr. Peter E. Wasberg are reflected throughout the O&M
20 Expense categories such as Production Expense, Transmission Expense, Distribution
21 Expense and others, based on the employees providing services in those expense
22 categories. Mr. Akerman will address the adjustments to compensation and employee
23 benefits expenses in his Direct Testimony.

24 **9. Corporate Allocations**

25 Q. HOW HAVE YOU REFLECTED ALLOCATIONS OF COSTS FROM OTTER TAIL
26 CORPORATION IN THE 2016 TEST YEAR?

27 A. Like Compensation and Employee Benefits expenses, Otter Tail Corporation costs
28 allocated to OTP are reflected in a number of categories of O&M expenses. OTP witness

1 Mr. Tommerdahl describes how Otter Tail Corporation costs allocated to OTP have been
2 reflected in the 2018 Test Year.

3 **B. Salaries, Wages, and Annual Incentive Compensation**

4 Q. WHAT TOPICS DO YOU DISCUSS IN THIS SUBSECTION OF YOUR DIRECT
5 TESTIMONY?

6 A. I will discuss the 2018 Test Year expenses of OTP's employee compensation and
7 benefits expense levels. Mr. Wasberg discusses the purposes, design and reasonableness
8 of these programs in his Direct Testimony.

9
10 Q. WHAT IS THE 2018 TEST YEAR EXPENSE FOR EMPLOYEE SALARIES, WAGES
11 AND ANNUAL INCENTIVE COMPENSATION?

12 A. The 2018 Test Year expense for employee salaries and wages including annual incentive
13 compensation is \$71,272,375 (OTP Total)/\$28,872,071 (OTP ND EST).

14
15 Q. HOW WERE 2018 TEST YEAR EMPLOYEE SALARIES AND WAGES
16 DEVELOPED?

17 A. As Mr. Wasberg explains in his Direct Testimony, the 2018 Test Year salary and wages
18 expense is based on 2018 budgeted amounts.

19
20 Q. DOES THE 2018 TEST YEAR INCLUDE THE FULL COST OF THE ANNUAL
21 INCENTIVE PLAN?

22 A. No. As Mr. Wasberg also explains in his Direct Testimony, that 2018 Test Year Key
23 Performance Award (KPA) costs are estimated 3 percent of eligible wages and annual
24 incentive costs are limited to 25 percent of wages for each individual.

25 **C. Pension Expenses and Effect on Revenue Requirement**

26 Q. WHAT TOPICS WILL YOU DISCUSS IN THIS SUBSECTION OF YOUR DIRECT
27 TESTIMONY?

28 A. In this subsection of my Direct Testimony, I will explain how pension expenses are
29 determined. All of the references to pension expenses included in this subsection of my

1 Direct Testimony are for 2018 Test Year O&M expenses only and do not include the
2 capitalized pension expense.

3
4 Q. WHAT IS THE 2018 TEST YEAR O&M PENSION EXPENSE?

5 A. The 2018 Test Year pension O&M expense is \$4,855,709 (OTP Total)/\$1,967,023 (OTP
6 ND EST).

7 **1. FAS 87 Pension Expenses**

8 Q. PLEASE SUMMARIZE THE BASIS FOR OTP'S 2018 TEST YEAR O&M PENSION
9 EXPENSE.

10 A. OTP's 2018 Test Year O&M pension expense was based on an estimate prepared by
11 Mercer, which provides actuarial services to OTP and Otter Tail Corporation. A copy of
12 that estimate is attached to the Direct Testimony of Mr. Wasberg as Exhibit __ (PEW-1),
13 Schedule 8. OTP will provide updated pension expense information to other stakeholders
14 and include the updated pension expense during the case.

15
16 Q. PLEASE SUMMARIZE THE ACCOUNTING BASIS FOR OTP'S PENSION PLAN.

17 A. The costs for OTP's pension plan are determined in accordance with ASC 715 (formerly
18 FAS 87). For convenience, I will continue to use the term FAS 87. Pension expense
19 represents an accrual for a future liability rather than the cash to pay benefits in a given
20 year.

21
22 Q. PLEASE PROVIDE AN OVERVIEW OF FAS 87.

23 A. FAS 87 is an accounting standard adopted in 1987 to govern employers' accounting for
24 pensions. Under FAS 87, annual pension cost is made up of several components,
25 including:

- 26 1) The present value of pension benefits that employees will earn during the current
27 year (annual service cost);
- 28 2) Increases in the present value of the pension obligation that plan participants have
29 earned in previous years (interest cost);
- 30 3) The EROA during the year; and

1 4) The recognition of prior-period gains or losses (e.g., amortization of investment
2 earnings different from those that had been assumed).
3

4 Q. HOW IS ANNUAL SERVICE COST CALCULATED?

5 A. The annual service cost is the actuarial present value of the projected retirement benefits
6 earned by plan participants in the current period. Actuarial assumptions are used to
7 reflect the time value of money (the discount rate) and the probability of payment
8 (mortality, turnover, early retirement, and so forth).
9

10 Q. HOW IS INTEREST COST CALCULATED?

11 A. The interest cost is determined as the increase in the plan's total pension benefit
12 obligation resulting from the fact that anticipated pension benefit payments are one year
13 closer to being paid from the pension plan.
14

15 Q. HOW IS EROA DETERMINED?

16 A. The EROA is determined based on the expected long-term rate of return on the market
17 value of pension plan assets. The product of the EROA multiplied by the amount of
18 assets in the pension trust provides an offset to the service costs and interest costs, and
19 therefore it reduces the pension expense.
20

21 Q. PLEASE SUMMARIZE THE THREE PRIMARY PENSION ASSUMPTIONS USED
22 TO DETERMINE OTP'S 2018 PENSION EXPENSE.

23 A. The primary pension assumptions are: (1) the discount rate; (2) the EROA; and (3) the
24 expected long-run wage increases over the period until benefits are paid. For OTP's
25 2018 pension expense, those assumptions are:
26

27 **Table 1**
28 **OTP Pension Expense Assumptions**

Discount Rate:	4.10%
EROA:	7.00%
Long-run average wage increase:	3.00%

1 These assumptions are based on an August 11, 2017 estimate from OTP's actuary.
2 Mercer. A copy of that estimate is attached to the Direct Testimony of Mr. Wasberg as
3 Exhibit __ (PEW-1), Schedule 8.
4

5 Q. WILL THE AUGUST 11, 2017 DETERMINE THE FINAL PENSION EXPENSE FOR
6 THE 2018 TEST YEAR?

7 A. No. Mercer will prepare another report based on December 31, 2017 data for the
8 Discount Rate, EROA, and Long-run average wage increase. That report will be
9 reviewed. When the Discount Rate, EROA, and Long-run average wage increase are
10 finalized, the resulting Pension Expense will be the actual Pension Expense for 2018.
11 OTP will provide copies of that report to the parties to this proceeding, which we expect
12 to receive in January or February 2018, and will update the FAS 106 and FAS 112
13 expenses accordingly.
14

15 Q. PLEASE DESCRIBE THE DECREASE IN THE PENSION DISCOUNT RATE.

16 A. Mercer's August 11, 2017 estimate of the pension discount rate for 2018 decreased from
17 4.60 percent in 2017 to 4.10 percent in 2018. The decrease reflected declining interest
18 rates on high quality bonds and led to an increase in pension expense of approximately
19 \$2.0 million. Mercer will issue a report based on market conditions as of December 31,
20 2017 in January or February. When the final discount rate is established, that discount
21 rate will be used to determine OTP's actual pension expense for 2018. OTP will provide
22 that report to parties to this proceeding when it becomes available.
23

24 Q. PLEASE DESCRIBE THE DECREASE IN THE EROA.

25 A. Mercer's August 11, 2017 estimate of the EROA for 2018 decreased from 7.50 percent in
26 2017 to 7.00 percent in 2018. The decrease reflected declining market trends and the
27 need to not understate expenses and led to an increase in pension expense of
28 approximately \$400,000. Mercer will issue a report based on market conditions as of
29 December 31, 2017 in January or February. When the final discount rate is established,

1 that discount rate will be used to determine OTP's actual pension expense for 2018. OTP
2 will provide that report to parties to this proceeding when it becomes available.

3
4 Q. PLEASE EXPLAIN THE REQUIREMENTS OF ASC 715 AND THE EFFECT ON
5 THE OTP 2018 O&M BUDGET.

6 A. In March 2017, the application of ASC 715 was revised by a Financial Accounting
7 Standards Board (FASB) Accounting Standards Update to include a prohibition on
8 capitalization of any interest component of non-service costs that are related to retirement
9 benefits. This prohibition was a change from prior practice in which allowed
10 capitalization of interest components of non-service costs related to retirement benefits.
11 This revision to ASC 715 had the effect of leaving no alternative for recovery of the
12 interest components of non-service costs other than recognition as a current expense.
13 Consistent with that ASC 715 requirement, OTP's 2018 O&M Budget has been
14 developed to reflect the treatment as O&M expense of all interest components of non-
15 service costs related to retirement benefits. The impact of ASC 715 on OTP's 2018
16 O&M Budget was approximately \$3 million.

17
18 Q. HAS FERC SUBSEQUENTLY ADDRESSED ASC 715?

19 A. Yes. In August 2017, FERC addressed ASC 715 in conversations with electric utility
20 representatives, and has indicated that a utility would be able to make an election to
21 either: (1) comply with ASC 715 (and expense all non-service costs that are related to
22 retirement benefits); or (2) continue to capitalize all components of retirement benefits as
23 had been approved by FERC. Once the election is made, a utility would not be allowed
24 to switch back. If a utility complies with ASC 715, there will be a difference between the
25 two methods which will need to be amortized.

26
27 Q. HAS FERC ISSUED FORMAL GUIDANCE?

28 A. No. These FERC positions have been communicated informally to electric utility
29 representatives, and from those representatives to the utilities. FERC staff is considering

1 issuance of some form of guidance to the industry, but no formal FERC guidance or
2 FERC position has been released.

3
4 Q. HAS OTP MADE THE ELECTION INFORMALLY DESCRIBED BY FERC?

5 A. No. While OTP intends to follow prior practice concerning capitalization of the interest
6 component of non-service costs related to retirement benefits, we are awaiting a formal
7 statement from FERC.

8
9 Q. HOW HAS OTP'S 2018 O&M BUDGET AND 2018 TEST YEAR REVENUE
10 REQUIREMENT BEEN AFFECTED?

11 A. OTP's 2018 O&M Budget and OTP's 2018 Test Year revenue requirement reflects
12 compliance with ASC 715, and the full interest component of non-service costs related to
13 retirement benefits has been expensed. No adjustment has been made to OTP's 2018
14 Test Year revenue requirement.

15 **2. Effect of Assets on Pension Expenses**

16 Q. DOES THE LEVEL OF ASSETS IN A COMPANY'S PENSION TRUST ALSO
17 AFFECT THE COMPANY'S PENSION EXPENSE?

18 A. Yes. As I summarized earlier, a company's current year's pension expense is directly
19 affected (reduced) by the product of the existing value of the assets in the company's
20 pension trust multiplied by the company's EROA. If the value of the pension assets is
21 higher, the product of the value of the pension assets multiplied by the EROA is greater.
22 Since this product is a reduction to the current pension expense, the level of expense in
23 the current period is reduced.

24
25 Q. DO THE LEVELS OF CONTRIBUTIONS BY A COMPANY TO ITS PENSION
26 TRUST ALSO AFFECT THE CURRENT YEAR PENSION EXPENSE?

27 A. Yes. The levels of contributions by a company to its pension plan trust also affect the
28 level of the pension plan assets and thus the level of offset available from the EROA in a
29 given year. As I will explain later in my Direct Testimony, OTP has made significant
30 contributions to the pension trust, which are prepayments of its funding obligations.

1 These prepayments have resulted in a substantial prepaid pension asset that also reduces
2 pension expense.

3
4 Q. DO THE ACTUAL EARNINGS ON THE PENSION ASSETS FROM PRIOR YEARS
5 AFFECT THE CURRENT YEAR PENSION EXPENSE?

6 A. Yes. The actual earnings from prior years on the pension assets affect the level of the
7 pension trust assets and thus the level of offset available from applying the EROA to the
8 pension asset, which provides a reduction in pension expense in a given year.

9
10 Q. DO GAINS AND LOSSES FROM PRIOR YEARS AFFECT CURRENT PENSION
11 COSTS?

12 A. Yes. Under FAS 87, pension asset gains and losses are the amounts by which actual
13 earnings either exceed the prior years' EROAs (as gains) or fall below the prior years'
14 EROAs (as losses). These gains or losses are phased in over a five-year period and then
15 amortized. Asset gains or losses are incorporated into the calculation of pension expense
16 over a period of five years, at the rate of 20 percent per year. Once a 20 percent portion
17 of a gain or loss is phased-in, it becomes part of the balance that is then amortized over a
18 number of years. As a result, a gain or loss is not fully recognized during the phase-in
19 period, which extends the period over which the gain or loss is recognized.

20 **3. Effect of OTP's Prepaid Pension Asset on Pension Expenses**

21 Q. DOES OTP HAVE A PREPAID PENSION ASSET AND DOES THAT ASSET
22 PROVIDE SUBSTANTIAL BENEFITS TO CUSTOMERS?

23 A. Yes. As I will explain further below, OTP has a pension asset that has resulted from its
24 significant contributions to its pension trust, and this pension asset provides substantial
25 benefits to customers, including a reduction in 2018 Test Year pension expense by \$1.71
26 million (OTP Total)/\$616,000 (OTP ND).

27

1 Q. PLEASE SUMMARIZE OTP’S RECENT CONTRIBUTIONS TO ITS PENSION
2 TRUST.

3 A. Since 2009, OTP contributed \$84 million (OTP Total), \$30.3 million (OTP ND) to its
4 pension trust, as shown on Table 2 below:

5

6

Table 2

7

OTP Pension Contributions 2019-2017

8

(OTP Total, \$ millions)

9

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	Total
OTP Pension Contribution	\$4	\$20	\$0	\$10	\$10	\$10	\$20	\$10	\$0	\$84

10

11 Q. WAS OTP REQUIRED TO MAKE THESE CONTRIBUTIONS?

12 A. No. These contributions are well above the funding requirements under the Employee
13 Retirement Income Security Act (ERISA).

14

15 Q. CAN OTP WITHDRAW SOME, OR ALL, OF THE PREPAID PENSION ASSET TO
16 FUND CAPITAL REQUIREMENTS, PAY EXPENSES OR INCREASE EARNINGS?

17 A. No. Federal law prohibits the withdrawal of any amounts from a pension trust fund
18 except for the payment of benefits and plan expenses. This prohibition applies even if the
19 assets in the pension trust exceed the funding requirements under ERISA.

20

21 Q. WHY DID OTP MAKE THESE CONTRIBUTIONS TO THE PENSION TRUST?

22 A OTP made these contributions for several reasons: (1) to preserve a steady and
23 conservative funding level of OTP’s pension obligation; (2) to mitigate the risk of
24 needing to make very large required contributions in future years; and (3) to take
25 advantage of the market recovery that has occurred since the 2008 market losses. These
26 contributions reflect OTP’s conservative approach to its pension obligations, which
27 provides substantial benefits to customers, as I will explain later in my Direct Testimony.

28

- 1 Q. WHAT IS THE AMOUNT OF OTP'S PREPAID PENSION ASSET?
- 2 A. The amount of OTP's 2018 Test Year prepaid pension asset is \$24.53 million (OTP
3 Total)/\$8.8 million (OTP ND) before the reduction for Accumulated Deferred Income
4 Taxes (ADIT). The calculation of that prepaid pension asset is set forth on
5 Exhibit___(CLP-1), Schedule 3.
6
- 7 Q. HOW WAS OTP'S PREPAID PENSION ASSET CALCULATED?
- 8 A. The pension asset is the excess of cumulative contributions over cumulative pension
9 expenses. OTP's annual pension expense was calculated in accordance with FAS 87.
10
- 11 Q. IS THE PREPAID PENSION ASSET INCLUDED IN RATE BASE?
- 12 A. Yes. The prepaid pension asset is included in rate base for three reasons: (1) including
13 the prepaid pension asset in rate base is consistent with standard regulatory treatment of
14 investor funded prepaid expenses; (2) including the prepaid pension asset in rate base is
15 consistent and symmetrical with the treatment that OTP has applied to FAS 106 and FAS
16 112 liabilities; and (3) the prepaid pension asset provides substantial benefits to
17 customers, including a reduction in current pension expenses and increased stability
18 resulting from having a lower level of future pension contributions.
19
- 20 Q. WAS A PREPAID PENSION ASSET INCLUDED IN OTP'S LAST NORTH
21 DAKOTA RATE CASE?
- 22 A. In our last North Dakota Rate Case, a zero balance was reflected in the prepaid pension
23 asset for the 2008 Test Year rate base. The zero balance, however, was not correct due to
24 an OTP internal accounting change that was not discovered until after the conclusion of
25 that case. As a result, OTP inadvertently omitted the Prepaid Pension expense from the
26 prepayment calculation and thus understated the rate base in the 2008 Test Year.
27
- 28 Q. HAS OTP'S PREPAID PENSION ASSET BEEN INCLUDED IN ANNUAL
29 REPORTS?

1 A. Yes. The prepaid pension asset (and its effect on pension expense) also has been
2 included in all our North Dakota Annual Reports.

3
4 Q. HAS OTP REDUCED THE PREPAID PENSION ASSET TO REFLECT ADIT
5 ASSOCIATED WITH THAT ASSET?

6 A. Yes. The ADIT balance offsets an addition to rate base (such as the prepaid pension
7 asset) and offsets the reduction to rate base (such as the liabilities relating to FAS 106 and
8 FAS 112). The ADIT associated with the prepaid pension asset is included in the overall
9 ADIT balance and reduces the OTP prepaid pension asset, as also shown on
10 Exhibit__(CLP-1), Schedule 3.

11
12 Q. HAVE YOU SUMMARIZED OTP’S PREPAID PENSION ASSET, THE
13 ASSOCIATED ADIT, AND THE RESULTING NET RATE BASE?

14 A. Yes. Table 3 below shows OTP’s prepaid pension asset, ADIT and net rate base impact
15 of \$14.85 million (OTP Total)/\$5.36 million (OTP ND).

16
17 **Table 3**
18 **Prepaid Pension Asset**
19 **(\$millions)**
20

Component	Non-Plant Rate Base Asset/ (Liability)	Associated ADIT Asset/(Liability)	Net Rate Base Impact Asset/(Liability)
Prepaid Pension Asset (OTP Total)	\$24.53	\$(9.67)	\$14.85
Prepaid Pension Asset (OTP ND)	\$8.85	\$(3.49)	\$5.36

21
22 Q. WHAT IS THE LEVEL OF OTP’S PENSION EXPENSE REDUCTION THAT
23 RESULTS FROM OTP’S PREPAID PENSION ASSET?

24 A. OTP’s prepaid pension asset reduces 2018 Test Year pension expense by \$1.71 million
25 (OTP Total)/\$616,000 (OTP ND). This reduction in pension expense results in
26 corresponding reductions to both OTP’s revenue requirement and OTP’s cost of service.

1 Q. PLEASE FURTHER EXPLAIN HOW THE PREPAID PENSION ASSET REDUCES
2 TEST YEAR PENSION EXPENSE.

3 A. OTP's prepaid pension asset reduces 2018 Test Year pension expense as a result of
4 applying the 7.00 percent 2018 EROA to the \$24.53 million (OTP Total)/\$8.8 million
5 (OTP ND) prepaid pension asset balance, which leads to pension earnings that are a
6 credit (reduction) to pension expense under FAS 87. As I have explained, OTP's annual
7 pension expense determined under FAS 87 includes a reduction in the pension expense
8 that results from expected earnings on the assets in the pension trust. The earnings that
9 are available to reduce pension expense are greater as a result of the OTP prepaid pension
10 asset. The additional earnings are based on the *entire* OTP pension trust asset balance
11 (the benefit of the EROA is not reduced by the ADIT reduction to rate base).
12

13 Q. HAVE YOU DETERMINED THE EXPENSE REDUCTION THAT RESULTS FROM
14 APPLYING THE EROA TO THE OTP PREPAID PENSION ASSET?

15 A. Yes. As shown on Exhibit___(CLP-1), Schedule 4, the 2018 OTP prepaid pension asset
16 will lead to a \$1.7 million (OTP Total)/\$620,000 (OTP ND) reduction in OTP's 2018
17 Test Year pension expense.
18

19 Q. HAVE YOU DETERMINED THE 2018 TEST YEAR REVENUE REQUIREMENT
20 RESULTING FROM THE PREPAID PENSION ASSET?

21 A. Yes. OTP's prepaid pension will lead to a \$604,000 revenue requirement (customer cost)
22 in the 2018 Test Year revenue requirement as a result of the increase in the Net Rate Base
23 (after reduction for the ADIT associated with the pension asset). The \$620,000 pension
24 expense reduction (customer benefit) exceeds the \$604,000 customer cost by \$16,000.
25 The calculation is also shown on Exhibit___(CLP-1), Schedule 4. This shows that OTP's
26 prepaid pension asset will not impose any added costs on customers even when
27 considered on a stand-alone basis. Further, there are other benefits to customers and
28 there is a significant net reduction to the 2018 Test Year revenue requirement resulting
29 from OTP's consistent rate base treatment of the pension asset and the FAS 106 and FAS
30 112 liabilities, as I will explain later in my Direct Testimony.

1 Q. ARE THERE OTHER BENEFITS TO CUSTOMERS THAT RESULT FROM OTP
2 PREPAID PENSION ASSET CONTRIBUTIONS?

3 A. Yes. The benefits of the prepaid pension asset will continue to increase from year to year
4 as the earnings on that asset accumulate and increase. Further, OTP customers benefit
5 from a reduction in the unfunded balance of the pension obligation because the risk of
6 being required to fund more in future years is also reduced.

7 **D. Net Effect of Prepaid Pension Asset and FAS 106 and 112 Liabilities**

8 Q. IS OTP'S POSITION REGARDING THE PENSION ASSET AND FAS 106 AND FAS
9 112 LIABILITIES INTERNALLY CONSISTENT AND SYMMETRICAL?

10 A. Yes. OTP has applied a consistent approach: (1) treating the accumulated contributions
11 to the pension plan in excess of accumulated pension expenses under FAS 87 as an
12 addition to rate base; and (2) treating the accumulated FAS 106 and FAS 112 expenses in
13 excess of accumulated payments as a reduction to rate base. The only other consistent
14 approach would be to not include in the rate base determination either the excess of
15 pension contributions or the excess of FAS 106 and 112 liabilities (which is the approach
16 the MPUC took). OTP's approach results in lower costs to customers, but an internally
17 consistent and symmetrical approach is essential as a matter of regulatory principle.
18

19 Q. PLEASE FURTHER EXPLAIN OTP'S APPROACH TO FAS 106 AND 112
20 LIABILITIES.

21 A. OTP's accumulated payments for FAS 106 and FAS 112 benefits are less than the
22 accumulated expense over the lives of the OTP retiree medical (FAS 106) and OTP post-
23 employment (FAS 112) benefit plans. As a result: (1) customers have made prepayments
24 for FAS 106 and FAS 112 costs; and (2) OTP has reflected the customer prepayments as
25 liabilities that reduce the OTP rate base. The situation regarding the pension is the
26 opposite, as I have explained.
27

28 Q. IS OTP'S PROPOSAL CONSISTENT WITH THE STANDARD RATEMAKING
29 TREATMENT OF PREPAYMENTS AND UNFUNDED LIABILITIES?

1 A. Yes. OTP is including the prepaid pension asset and reduced rate base for the customer-
 2 funded prepaid FAS 106 and FAS 112 liabilities, which is the standard ratemaking
 3 treatment of both. Both rate base additions and rate base reductions are also adjusted
 4 (partially offset) for income tax effects through ADIT as shown on Exhibit _(CLP-1),
 5 Schedule 5 and Exhibit_(CLP-1), Schedule 6.

7 Q. WHAT IS THE 2018 TEST YEAR NET RATE BASE IMPACT OF INCLUDING THE
 8 PREPAID PENSION ASSET AND 106 AND FAS 112 LIABILITIES?

9 A. Table 4 below shows the net rate base impact of including the 2018 Test Year prepaid
 10 pension asset, FAS 106 and FAS 112 balances is \$13.6 million (OTP Total)/\$9.2 million
 11 (OTP ND) decrease to OTP’s 2018 Test Year rate base:

13 **Table 4**
 14 **2018 Test Year Rate Base Impact of**
 15 **Prepaid Pension Asset, FAS 106 and FAS 112 Liabilities**
 16 **(OTP ND)**
 17 **(\$millions)**

Component	Non-Plant Rate Base Asset/ (Liability)	Associated ADIT Asset/(Liability)	Net Rate Base Impact Asset/(Liability)
Prepaid Pension Asset	\$ 8,852	(\$3,492)	\$ 5,360
FAS 106 Liability	(21,833)	7,681	(14,152)
FAS 112 Liability	(579)	170	(409)
Total Net Impact	(\$13,560)	\$ 4,359	(\$9,201)

20 Q. WHAT IS THE SIGNIFICANCE OF THE NET IMPACT BEING A REDUCTION TO
 21 RATE BASE?

22 A. The \$9.2 million Net Impact reduction in rate base will reduce the 2018 Test Year
 23 revenue requirement by approximately \$1.0 million (OTP ND), as shown on
 24 Exhibit__(CLP-1), Schedule 7. Customers also benefit from the \$620,000 decrease in
 25 the OTP ND pension expense that I explained earlier. (The full amount of that \$620,000
 26 decrease represents a customer benefit when the net impact of the pension asset and FAS
 27 106 and 112 liabilities are considered because the “cost” of the pension asset has been
 28 accounted for in the determination of the Net Impact rate base effect.)

1 Q. WERE THE PENSION ASSET AND FAS 106 AND FAS 112 LIABILITIES
2 INCLUDED IN THE RATE BASE IN OTP'S RECENT MINNESOTA RATE CASE?

3 A. No. In OTP's recent Minnesota rate case, the Minnesota Public Utilities Commission
4 (MPUC) took a completely different, but internally consistent, position of not including
5 *either* OTP's prepaid pension asset or OTP's retiree medical (FAS 106) and OTP post-
6 employment (FAS 112) liabilities in rate base. This decision was contrary to OTP's
7 recommendation that both the prepaid pension asset and the FAS 106 and FAS 112
8 liabilities be reflected in rate base which would have reduced the Minnesota revenue
9 requirement, just as OTP's recommendation in this case reduces the 2018 Test Year
10 revenue requirement.
11

12 Q. WHAT WAS THE EFFECT OF THE MPUC DECISION?

13 A. The MPUC's decision resulted in a net increase to OTP's rate base and revenue
14 requirement. The MPUC's position was internally consistent and symmetrical, which is
15 essential. It is also the only internally consistent and symmetrical alternative to OTP's
16 position, but it would increase the 2018 Test Year revenue requirement, and OTP does
17 not recommend that alternative.

18 **E. Other Benefits Expenses**

19 Q. WHAT IS THE 2018 TEST YEAR EXPENSE FOR EMPLOYEE GROUP
20 INSURANCE BENEFITS?

21 A. The 2018 Test Year O&M cost for employee group insurance benefits, which includes
22 active medical, dental, life insurance and long-term disability (LTD), is \$9,041,991 (OTP
23 Total)/\$3,666,105 (OTP ND EST).
24

25 Q. HOW WERE 2018 TEST YEAR EMPLOYEE GROUP INSURANCE BENEFITS
26 DETERMINED?

27 A. As Mr. Wasberg explains in his Direct Testimony, the 2018 Test Year employee group
28 insurance benefits expense is based on 2018 budgeted amounts. Mr. Wasberg also
29 discusses the development of the budgeted amounts and the steps taken to control these
30 expenses.

1 Q. WHAT IS THE 2018 TEST YEAR EXPENSE FOR FAS 106 AND FAS 112
2 BENEFITS?

3 A. The 2018 Test Year cost for FAS 106 benefits is \$1,253,086 (OTP Total)/\$507,619 (OTP
4 ND EST). The 2018 Test Year cost for FAS 112 benefits is \$567,805 (OTP
5 Total)/\$230,015 (OTP ND EST).
6

7 Q. HOW WERE 2018 TEST YEAR FAS 106 AND FAS 112 EXPENSES DETERMINED?

8 A. As Mr. Wasberg explains in his Direct Testimony, the 2018 Test Year FAS 106 and FAS
9 112 expenses were based on an estimate prepared by Mercer, a copy of which is attached
10 to his Direct Testimony as Exhibit __ (PEW-1), Schedule 8. The decrease in the discount
11 rate reflected in the August 11, 2017 Mercer estimate increased FAS 106 expenses by
12 approximately \$300,000.
13

14 Q. WILL THE AUGUST 11, 2017 MERCER ESTIMATE DETERMINE THE FINAL
15 FAS 106 AND FAS 112 EXPENSES FOR THE 2018 TEST YEAR?

16 A. No. Similar to the Pension Expense, Mercer will prepare another report based on
17 December 31, 2017 data for the Discount Rate and other FAS 106 and FAS 112
18 assumptions for 2018. OTP will provide copies of that report to the parties to this
19 proceeding, which we expect to receive in January or February, 2018, and will update the
20 FAS 106 and FAS 112 expenses accordingly.
21

22 Q. WHAT IS THE 2018 TEST YEAR EXPENSE FOR THE OTP DEFINED
23 CONTRIBUTION AND 401(k) MATCH?

24 A. The 2018 Test Year cost for the OTP defined contribution plan is \$766,245 (OTP Total)/
25 \$310,402 (OTP ND EST). The 2018 Test Year cost for the OTP 401k match is
26 \$1,365,216 (OTP Total)/ \$553,042 (OTP ND EST).
27

1 Q. HOW WAS THE 2018 TEST YEAR EXPENSE FOR THE OTP DEFINED
2 CONTRIBUTION AND 401K MATCH DETERMINED?

3 A. As Mr. Wasberg explains in his Direct Testimony, the 2018 Test Year OTP defined
4 contribution plan and the 401k match are based on 2018 budgeted amounts.

5 **V. CONCLUSION**

6 Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

7 A. Yes, it does.

Mrs. Christine L. Petersen, CPA
Financial/Rates Analyst, Business Planning/Regulatory Accounting
Otter Tail Power Company
215 South Cascade Street
Fergus Falls, Minnesota 56537
218-739-8541

CURRENT RESPONSIBILITIES: (May 2010 to Present)

Responsible for financial analysis related to setting rates and overall cost recovery, including preparing cost of service studies which is used to determine utility revenue requirement as well as the basis for rate design. In conjunction with the preparation of the cost of service studies, will need to determine how to handle new accounting rules as they arise and determine overall utility returns for actual and forecast years. Prepare class cost of service studies for rate design. Analyze and investigate study results. Prepare exhibits, testimony and answer information requests during rate cases. Will provide internal business consulting services upon request. Assist in calculation of budget/forecast information and aid in implementation of specialized accounting procedures as directed by regulatory agencies or orders. Perform miscellaneous revenue requirement and other financial analysis as they arise.

PREVIOUS POSITIONS:

Otter Tail Power Company

2010 – Present Financial/Rates Analyst, Business Planning/Regulatory
Accounting

Carlson Highland

2008 – 2010 Governmental Auditor

EDUCATIONAL / CERTIFICATIONS

Moorhead State University-Moorhead, B.S.
Major in Accounting

Certified Public Accountant (CPA)

OTTER TAIL POWER COMPANY
 Electric Utility - State of North Dakota
 SCHEDULE OF OPERATIONS AND MAINTENACE EXPENSE

Line No.	Description	(A)	(B)	(C)	(D)
		Base Total Utility	Base ND Jurisdiction	Adjustments	Proposed Test Year ND
Proposed Test Year 2018					
<u>OPERATING EXPENSES</u>					
1	Production Expenses	\$161,876,335	\$60,104,536	(\$347,737)	\$59,756,799
2	Transmission Expenses	\$35,311,843	13,507,453	0	13,507,453
3	Distribution Expenses	\$16,917,384	7,680,921	0	7,680,921
4	Customer Accounting Expenses	\$13,849,926	6,091,579	0	6,091,579
5	Customer Service and Information Expenses	\$11,097,740	1,382,509	0	1,382,509
6	Sales Expenses	\$273,627	22,472	200,000	222,472
7	Administration and General Expenses	\$50,400,273	20,112,229	(515,613)	19,596,616
8	Charitable Contributions	\$0	0	0	0
9	Depreciation Expense	\$54,316,572	20,716,262	709,039	21,425,301
10	General Taxes	<u>\$15,375,197</u>	<u>4,902,302</u>	<u>3,590</u>	<u>4,905,891</u>
11	TOTAL OPERATING EXPENSES	<u>\$359,418,897</u>	<u>\$134,520,262</u>	<u>\$49,279</u>	<u>\$134,569,541</u>

Prepaid Pension
 (thousands)

Line No.	Month	Year	Balance	ADIT	Net (Total)
1	December	2017	32,422	(12,782)	19,640
2	January	2018	31,109	(12,266)	18,843
3	February	2018	29,792	(11,747)	18,045
4	March	2018	28,478	(11,230)	17,248
5	April	2018	27,163	(10,713)	16,450
6	May	2018	25,847	(10,195)	15,652
7	June	2018	24,533	(9,678)	14,855
8	July	2018	23,218	(9,161)	14,057
9	August	2018	21,902	(8,643)	13,259
10	September	2018	20,586	(8,125)	12,461
11	October	2018	19,270	(7,607)	11,663
12	November	2018	17,954	(7,089)	10,865
13	December	2018	16,636	(6,571)	10,065
Total			318,910	(125,807)	193,103
13 Mo ave			24,532	(9,677)	14,854
OTP ND			8,852	(3,492)	5,360

Calculation of Customer Benefits from Prepaid Pension Asset (thousands)

Line No.		Ave balance	ADIT	Net (Total)	Net (ND)
1	Expected Return on Plan Assets (EROA) @ 7.00% times 13 mo ave balance		\$24,532	\$1,717	\$620
2	13 Month Average Prepaid Pension Balance (see CLP-1, Sch. 3)	\$24,532	(\$9,677)	\$14,854	\$5,177
3	Revenue Requirement @ 7.97% ROR	1,955	(771)	1,184	413
4	Tax impact	807	(318)	489	14
5	Total Revenue Impact on Prepaid Pension Asset	2,762	(1,090)	1,673	426
6	Revenue Requirement Impact of prepaid pension less costs offset by prepaid pension asset			(\$45)	(\$193)

Retiree Medical Liability (FAS 106)
 (thousands)

Line No.	Month	Year	Balance	ADIT	Net (Total)
1	December	2017	(63,000)	22,197	(40,802)
2	January	2018	(62,614)	22,046	(40,568)
3	February	2018	(62,228)	21,894	(40,334)
4	March	2018	(61,714)	21,742	(39,972)
5	April	2018	(61,328)	21,590	(39,738)
6	May	2018	(60,942)	21,438	(39,504)
7	June	2018	(60,428)	21,286	(39,142)
8	July	2018	(60,043)	21,135	(38,908)
9	August	2018	(59,657)	20,983	(38,674)
10	September	2018	(59,143)	20,831	(38,312)
11	October	2018	(58,757)	20,679	(38,078)
12	November	2018	(58,371)	20,527	(37,844)
13	December	2018	(58,369)	20,376	(37,994)
Total			(786,594)	276,724	(509,869)
13 Mo ave			(60,507)	21,286	(39,221)
OTP ND			(21,833)	7,681	(14,152)

Post Employmnt Benefits Liability (FAS 112)
 (thousands)

Line No.	Month	Year	Balance	ADIT	Net (Total)
1	December	2017	(1,402)	391	(1,011)
2	January	2018	(1,436)	404	(1,031)
3	February	2018	(1,470)	418	(1,052)
4	March	2018	(1,503)	431	(1,073)
5	April	2018	(1,537)	444	(1,093)
6	May	2018	(1,571)	458	(1,114)
7	June	2018	(1,605)	471	(1,134)
8	July	2018	(1,639)	484	(1,155)
9	August	2018	(1,673)	498	(1,175)
10	September	2018	(1,707)	511	(1,196)
11	October	2018	(1,741)	524	(1,217)
12	November	2018	(1,775)	538	(1,237)
13	December	2018	(1,809)	551	(1,258)
Total			(20,867)	6,122	(14,745)
13 Mo ave			(1,605)	471	(1,134)
OTP ND			(579)	170	(409)

OTP ND Net Impact of Pension Asset and FAS 106 and FAS 112 Liabilities

(thousands)

OTP ND Net Impact

Line No.		Non-Plant Rate Base	Associated ADIT	Net Rate Base Impact
1	Total Net Rate Base Impact	(\$13,560)	\$4,359	(\$9,201)
2	Rate Base Revenue Requirement Factor			11.26%
3	Total Revenue Impact (OTP ND)			(\$1,036)