Surrebuttal Testimony
Dylan W. D'Ascendis

Before the North Dakota Public Service Commission
State of North Dakota

In the Matter of the Application of Northern States Power Company
for Authority to Increase Rates for Natural Gas Service in North Dakota

Case No. PU-21-381
Exhibit___(DWD-3)

Rate of Return

May 6, 2022

76 PU-21-381 Filed 05/06/2022 Pages: 25
Surrebuttal Testimony of Dylan W. D'Ascendis
Northern States Power Company

Table of Contents

I. INTRODUCTION, PURPOSE, AND SUMMARY

Q. PLEASE STATE YOUR NAME, OCCUPATION AND BUSINESS ADDRESS.

A. My name is Dylan W. D'Ascendis. I am employed by ScottMadden, Inc. as Partner. My business address is 3000 Atrium Way, Suite 241, Mount Laurel, NJ 08054.

Q. ON WHOSE BEHALF ARE YOU SUBMITTING THIS SURREBUTTAL?

A. I am submitting this surrebuttal testimony (referred to throughout as my "Surrebuttal Testimony") before the North Dakota Public Service Commission (Commission) on behalf of Northern States Power, a Minnesota corporation (NSP or the Company).

Q. DID YOU FILE DIRECT AND REBUTTAL TESTIMONIES IN THIS PROCEEDING?

A. Yes, I did.

Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

A. The purpose of my Surrebuttal Testimony is to respond to the surrebuttal testimonies of Dr. Marlon F. Griffing, who testifies on behalf of the North Dakota Public Service Commission Advocacy Staff (Staff) and William H. Malcom, who testifies on behalf of the American Association of Retired Persons (AARP) as they relate to the Company's return on common equity (ROE) on its North Dakota jurisdictional rate base.

Q. PLEASE SUMMARIZE YOUR POSITIONS IN THIS PROCEEDING.

A. My primary position is that the appropriate ROE attributable to the Company is 10.50%, which is based on the results of several well-tested ROE models applied to a proxy group of gas distribution utilities similar in total risk to NSP which were then adjusted to reflect the Company's unique risks compared to the proxy group. A summary of my ROE model results and relative risk adjustments are shown on Table 1, below:

Table 1
Summary of Common Equity Cost Rates[1]

Discounted Cash Flow Model	10.06%
Risk Premium Model	10.58%
Capital Asset Pricing Model	11.76%
Cost of Equity Models Applied to Comparable Risk, Non-Price Regulated Companies	12.72%
Indicated Range of Common Equity Cost Rates Before Adjustments	10.06% - 12.72%
Size Adjustment	0.50%
Credit Risk Adjustment	0.00%
Flotation Cost Adjustment	0.14%
Indicated Range of Common Equity Cost Rates after Adjustment	10.70% - 13.36%
Recommended Cost of Common Equity	10.50%

My updated model results, which reflect current and expected capital markets,[2] indicate a higher investor-required return since the initial

1 Exhibit__(DWD-2), Schedule 1 (D'Ascendis Rebuttal Testimony).
2 D'Ascendis Rebuttal Testimony, at 5-13.

Company filing, much like Dr. Griffing's updated results exceed his initial results. While I maintain my recommended 10.50% ROE for NSP, my model results indicate an ROE somewhat higher than my recommendation. On the other hand, Dr. Griffing's increased ROE recommendation still does not rise to the level of being a reasonable rate of return for NSP at this time.

My secondary position is that the Company's requested capital structure, which contains 47.03% long-term debt, 0.43% short-term debt, and 52.54% common equity is appropriate, as it finances the Company's operations and it is in line with its industry peers.[3]

Q. PLEASE SUMMARIZE YOUR CONCLUSIONS DRAWN FROM THIS SURREBUTTAL TESTIMONY.

A. None of Dr. Griffing's or Mr. Malcolm's surrebuttal testimonies have caused me to change either of my positions as presented above.

Q. PLEASE SUMMARIZE DR. GRIFFING'S ROE RECOMMENDATION.

A. In his direct testimony Dr. Griffing recommended a 9.40% ROE,[4] which he updates in his surrebuttal testimony to 9.54%.[5] His recommendation is based on the results of his Constant Growth Discounted Cash Flow (DCF), multi-stage DCF, and CAPM results, based on market return data from *Value Line Investment Survey (Value Line)* and I/B/E/S. To each of

3 D'Ascendis Direct Testimony, at 25-26, D'Ascendis Rebuttal Testimony, at 37-39.
4 Griffing Direct Testimony, at 3.
5 Griffing Surrebuttal Testimony, at 3.

his DCF results Dr. Griffing applied 40% weight and to each of his CAPM analyses he applied 10% weight.[6] Dr. Griffing's analytical results range from 8.72% (multi-stage DCF) to 11.77% (I/B/E/S CAPM).[7] Those results overlap with my recommended ROE of 10.50% and range of 10.70% to 13.36%.[8]

Q. PLEASE SUMMARIZE YOUR RESPONSE TO DR. GRIFFING'S SURREBUTTAL TESTIMONY.

A. Although Dr. Griffing updates his analyses for more recent data, he has not changed the application of the models. As such, the issues I raised in my Rebuttal Testimony related to Dr. Griffing's application of his analytical models remain relevant.[9] I also continue to disagree with Dr. Griffing's use of the multi-stage DCF model.

Specific to his surrebuttal testimony, I do not agree with Dr. Griffing's reasoning for changing the weights he applied to his model results to derive his recommended ROE. Had Dr. Griffing excluded his multi-stage DCF results and applied equal weighting to his DCF and CAPM results, his recommendation would have been 10.47%, only three basis points below my recommendation.[10] I then address Dr. Griffing's responses to my critiques of his analyses.

6 Griffing Surrebuttal Testimony, at 12-13.
7 Griffing Surrebuttal Testimony, at 7-8, 12.
8 D'Ascendis Rebuttal Testimony, at 4.
9 D'Ascendis Rebuttal Testimony, at 17-29.
10 As illustrated in Table 4 below.

Q. PLEASE SUMMARIZE YOUR RESPONSE TO MR. MALCOLM'S SURREBUTTAL TESTIMONY.

A. I highly disagree with Mr. Malcolm's suggestion that authorized returns of 9.20% and 9.30% for Public Service Company of Colorado's (PSCO) natural gas and electric operations are relevant benchmarks for NSP's ROE in this proceeding. Settlements for related operating companies in other regulatory jurisdictions during different time frames have no bearing on the investor required cost of capital for NSP's North Dakota gas operations currently.

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

A. The remainder of my Surrebuttal Testimony is organized as follows:

- *Section II* – Provides my response to Staff Witness Griffing;
- *Section III* – Provides my response to AARP Witness Malcolm; and
- *Section IV* – Presents my conclusions.

II. RESPONSE TO STAFF WITNESS GRIFFING

Q. PLEASE SUMMARIZE DR. GRIFFING'S SURREBUTTAL TESTIMONY.

A. Dr. Griffing first updates his constant growth and multi-stage discounted cash flow analyses and his CAPM analyses based on recent data, which he uses to inform his ROE recommendation of 9.54%. Dr. Griffing then responds to certain issues raised in my Rebuttal Testimony. Dr. Griffing maintains his recommended hypothetical capital structure which contains

52.00% common equity, 47.57% long-term debt, and 0.43% short-term debt.

A. Updated Analytical Results and Recommended ROE

Q. DID DR. GRIFFING CHANGE HIS APPLICATION OF HIS ANALYTICAL MODELS IN HIS SURREBUTTAL TESTIMONY?

A. No, he did not. Although Dr. Griffing updates his analyses for more recent data, he has not changed the application of the models. As such, the issues I raised in my Rebuttal Testimony related to Dr. Griffing's application of his analytical models remain relevant.[11] I also continue to disagree with Dr. Griffing's use of the multi-stage DCF model.

Q. WHAT ARE YOUR OBSERVATIONS RELATED TO DR. GRIFFING'S UPDATED RECOMMENDED ROE?

A. Consistent with the analytical results in my Rebuttal Testimony, Dr. Griffing's analytical results in his surrebuttal testimony point to a directionally higher ROE. The higher analytical results translate to a 14-basis point increase in Dr. Griffing's ROE recommendation.

Q. DOES DR. GRIFFING CHANGE THE WEIGHTING OF HIS MODEL RESULTS?

A. Yes, he does. In his direct testimony Dr. Griffing gave 37.5% weight to each of his DCF results, 15% weight to his *Value Line* CAPM result, and 10% weight to his I/B/E/S CAPM results.[12] In his surrebuttal testimony

11 D'Ascendis Rebuttal Testimony, at 17-29.
12 Griffing Direct Testimony, at Exhibit MFG-16, Schedule 1.

Dr. Griffing applied 40% weight to each of his DCF results and 10% to each of his CAPM results.[13] Applying the same weighting as Dr. Griffing did in his direct testimony, using the analytical results in his surrebuttal testimony, would result in a recommended ROE of 9.66%.

Table 2

Dr. Griffing Analytical Results with Direct Testimony Weighting

Model	Weight	Result	Weighted Result
Constant Growth DCF	37.50%	9.29%	3.48%
Multi-Stage DCF	37.50%	8.72%	3.27%
Value Line CAPM	15.00%	11.54%	1.73%
I/B/E/S CAPM	10.00%	11.77%	1.18%
Weighted Average Result			9.66%

Q. WHY DID DR. GRIFFING CHANGE THE WEIGHTS HE APPLIED TO HIS ANALYTICAL RESULTS?

A. Dr. Griffing gave less weight to his CAPM results in his surrebuttal testimony because "the I/B/E/S and Value Line CAPM ROE results were about 1.25 percent and 1.00 percent, respectively, greater than the single highest ROE authorized for a natural-gas utility in the United States in the 2019-2021 span."[14]

Q. DO YOU AGREE WITH DR. GRIFFING'S REASONING?

A. No, I do not. As discussed in my Rebuttal Testimony, authorized ROEs are a lagging indicator of investor-required returns and, as such, cannot

13 Griffing Surrebuttal Testimony, at Exhibit MFG-S-6, Schedule 1.
14 Griffing Direct Testimony, at 43.

reflect investor-required returns in a dynamic economic environment as we are currently experiencing.[15] Additionally, Dr. Griffing's reasoning is inconsistent with his argument that authorized ROEs are "not a good substitute for current, forward-looking ROE analyses."[16] Specifically, Dr. Griffing states:

> Recently authorized ROEs reflect the results of rate cases conducted in a variety of environments and at different times. Test years, conditions in capital markets, general economic indicators such as inflation rates, and so forth for previous rate cases can be different and become outdated when compared with these factors for a current rate case. Therefore, recently authorized ROEs should serve only to establish whether a current ROE result is reasonably close to what has happened, not be a substitute for forward-looking analysis based on current conditions.[17]

Given his own correct assessment of the applicability of authorized returns on the investor-required return, Dr. Griffing should not have used them as a limit on his model results.

Q. WHAT WOULD DR. GRIFFING'S RECOMMENDED ROE BE IF HE EQUALLY WEIGHTED HIS ANALYTICAL RESULTS?

A. First, as discussed in detail in my Rebuttal Testimony, I do not agree that the multi-stage DCF model is appropriate to rely on in this proceeding.[18] As such, I have not included it in calculating Dr. Griffing's adjusted recommended ROE. As shown in Table 3, giving equal weight to the

---

15 D'Ascendis Rebuttal Testimony, at 5-6.
16 Griffing Surrebuttal Testimony, at 12.
17 Griffing Surrebuttal Testimony, at 12.
18 D'Ascendis Rebuttal Testimony, at 19-23.

three remaining analytical results produces a range of 9.29% to 11.77%, with an average of 10.87%. As shown in Table 4, applying 50% weight to the constant growth DCF results and the average of the CAPM results produces a range of 9.29% to 11.66%, with an average of 10.47%. Those results overlap with my recommended range and a 10.47% ROE is only three basis points below my ROE recommendation.

Table 3

Dr. Griffing Adjusted ROE Recommendation

Model	Weight	Result	Weighted Result
Constant Growth DCF	33.33%	9.29%	3.10%
Value Line CAPM	33.33%	11.54%	3.85%
I/B/E/S CAPM	33.33%	11.77%	3.92%
Weighted Average Result			10.87%

Table 4

Dr. Griffing Adjusted ROE Recommendation

Model	Weight	Result	Weighted Result
Constant Growth DCF	50.00%	9.29%	4.65%
Average CAPM	50.00%	11.66%	5.83%
Weighted Average Result			10.47%

Q. DOES DR. GRIFFING'S CHANGE IN WEIGHTING HIS MODEL RESULTS FROM HIS DIRECT TO HIS SURREBUTTAL COMPOUND ANY EXISTING CONCERNS?

A. Yes, it does. As mentioned in my Rebuttal Testimony, Dr. Griffing incorporated a size-adjusted CAPM and full flotation costs for NSP in its last electric rate case (Docket No. PU-20-441) but does not in this proceeding, which serves to lower his recommendation.[19] Dr. Griffing's change in weighting his models from his direct to his surrebuttal also serves to lower his recommendation.

As discussed above, Dr. Griffing's justification for changing the weighting of his model results is in conflict with his own statements, and should be dismissed by the Commission. Likewise, Dr. Griffing's justifications for changing his positions regarding the size and flotation cost adjustment and his flotation cost are without merit and should be dismissed by the Commission.

B. Application of Multi-Stage Discounted Cash Flow Model

Q. PLEASE SUMMARIZE DR. GRIFFING'S RESPONSE TO YOUR CRITICISM OF HIS MULTI-STAGE DCF MODEL.

A. Dr. Griffing states that three- to five-year earnings per share (EPS) growth rates are currently elevated due to the effects of the COVID-19 pandemic. He also states that because he relied on EPS growth rates for the period 2022-2026 and gross domestic product (GDP) growth rates for the period 2027-2050, 2027 represents the transition year of his multi-stage DCF model.[20]

19 D'Ascendis Rebuttal Testimony, at 30-32
20 Griffing Surrebuttal Testimony, at 15-17.

Q. WHAT IS YOUR RESPONSE TO DR. GRIFFING'S ASSUMPTION THAT EPS GROWTH RATES ARE ABNORMALLY HIGH?

A. From a practical standpoint, for expected growth rates to be abnormally high, as Dr. Griffing suggests, the EPS for the proxy companies would necessarily need to have been lower than it otherwise would be without the market dislocation. By way of a hypothetical example, assuming a 2019 EPS of $1.00 for Company A, and an expected EPS of $1.10 three to five years in the future, would result in an expected growth rate of 10.00%. Now assuming that the EPS for Company A falls to $0.80 in 2020 and expected EPS of $1.10 remains, the expected growth rate increases to 37.50%. That is, for Dr. Griffing's assumption that EPS growth rates for the proxy companies are higher than they should be due to the effects of the COVID-19 pandemic to be correct, there would have needed to be a decrease in the EPS for those companies. As shown in my Rebuttal Testimony, that was not the case.[21]

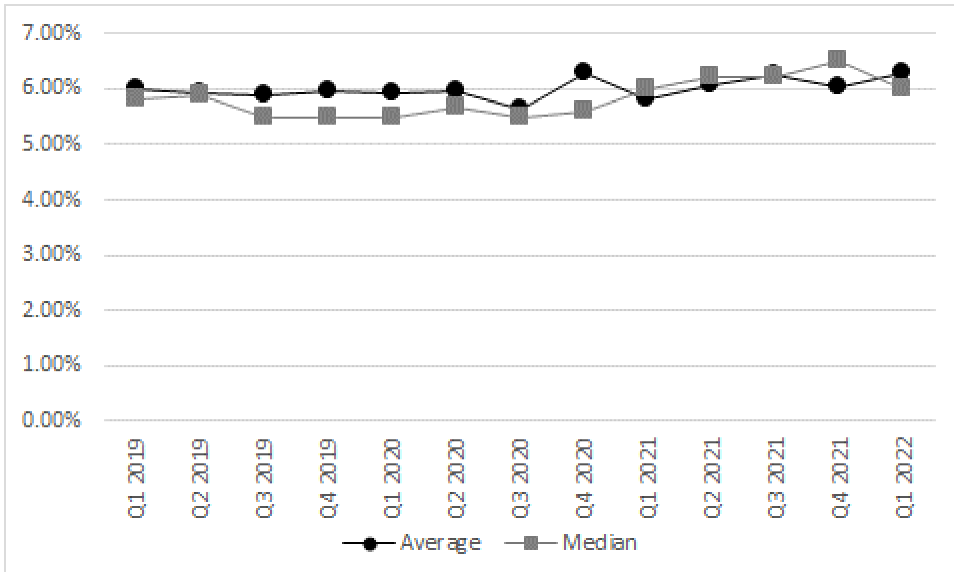
Furthermore, I also considered how EPS growth rates for the proxy companies changed from Q1 2019 to Q1 2022. I collected the EPS growth rates from *Value Line*, Zacks, and Yahoo! Finance as of the release date of the *Value Line* report in each quarter. Chart 1, below, presents the average and median growth rates for each of those periods. As shown in Chart 1, although there has been some variation over the observation period, the average and median growth rates have generally been around

21 D'Ascendis Rebuttal Testimony, at 20.

6.00%. The most recent observations (Q1 2022) are also highly consistent with the observations from Q1 2019.

Chart 1

Average EPS Growth Rates[22]



Q. DO YOU AGREE WITH DR. GRIFFING'S CONCLUSION THAT THE TRANSITION YEAR OF HIS MULTI-STAGE DCF ANALYSIS IN HIS DIRECT TESTIMONY IS 2027?

A. No, I do not. I agree with Dr. Griffing that he has relied on EPS growth rates that end in 2026 and GDP growth rates that begin in 2027 in his direct testimony. However, Dr. Griffing weighted his EPS growth rate estimates by two-thirds and his GDP growth rate estimate by one-third. Those weights imply that at some point in the future the model transitions from the first stage (EPS growth rates) to the second stage (GDP growth

22 Source: *Value Line*, Zacks, and Yahoo! Finance. Excludes EPS growth rates from *Value Line* for Northwest Natural Gas Company due to relatively high growth rate estimates in 2019 and 2020.

rate). To ensure a transition year of 2027, Dr. Griffing would have had to rely on a model similar to the one described on pages 19 and 20 in my Rebuttal Testimony; where the first five years rely on growth equal to the EPS growth rate estimates and each subsequent year growth is equal to the expected growth rate in GDP. Dr. Griffing has not performed such an analysis. As such, he has not provided any support for the implied transition year between his growth rate estimates that arises due to his weighting of those growth rates.

C. Application of Capital Asset Pricing Model

Q. WHAT IS YOUR RESPONSE TO DR. GRIFFING'S ARGUMENT THAT CURRENT BOND YIELDS ARE THE APPROPRIATE MEASURE OF THE RISK-FREE RATE?

A. As discussed in my Rebuttal Testimony, the cost of capital and ratemaking are inherently forward-looking. Given that, expected interest rates are appropriate for cost of capital purposes.[23]

Q. DO YOU HAVE ANY CONCERNS WITH DR. GRIFFING'S CALCULATION OF THE MARKET RETURN?

A. Yes, I do. As discussed in my Rebuttal Testimony the market return is meant to reflect the return of all companies in the market.[24] The calculation of the market return is supposed to determine the projected return on the market, which is the sum of income returns (dividends) and capital appreciation. Companies that do not pay dividends still contribute

23 D'Ascendis Rebuttal Testimony, at 25.
24 D'Ascendis Direct Testimony, at 26.

to the total return of the market and therefore must be reflected. At any given time the overall market will have companies that have relatively high and low growth rates.

Further, Dr. Griffing's assertion that removing certain companies from the calculation of the market return is appropriate "because NSP would not be competing for capital against such outliers,"[25] is misguided. Again, the purpose of the market return is to estimate the return on the overall market, not companies that compete against NSP. As Dr. Griffing notes in his Direct Testimony, the CAPM is calculated as the risk-free rate plus a return "that reflects the <u>additional rate of return earned by other companies in the broad equity market</u> adjusted for the risk of the subject company relative to the risk of an average company in the market."[26] That is, the market return reflects the return on the "broad equity market," not a subset of the market or companies that compete with the subject company.

Q. WHAT IS YOUR RESPONSE TO DR. GRIFFING'S ASSERTION THAT COMPARING THE BETA COEFFICIENT (BETA) OF THE S&P 500 AND DR. GRIFFING'S GROUP OF COMPANIES SUGGESTS THAT THE COMPANIES USED IN HIS MARKET RETURN ESTIMATE IS REASONABLE?

A. The betas provided by Dr. Griffing do not provide any value. In my Rebuttal Testimony I raised the concern that there is a mismatch between the estimate of beta provided by *Value Line* and Dr. Griffing's market

25 Griffing Surrebuttal Testimony, at 19.
26 Griffing Direct Testimony, at 13. Emphasis added.

return estimates.[27] As Dr. Griffing notes, the beta represents "the risk of the subject company relative to the risk of an average company in the market."[28] Because the beta is a relative measure, relying on betas from *Value Line*, which are relative to the overall market, may not be appropriate because Dr. Griffing's market return estimate does not measure the return of the overall market. Dr. Griffing's comparison of betas for the S&P 500 and his group of companies does not refute that mismatch in data.

D. Flotation Costs

Q. WHAT IS YOUR RESPONSE TO DR. GRIFFING'S TESTIMONY AS IT RELATES TO FLOTATION COSTS?

A. As discussed in my Rebuttal Testimony, flotation costs remain part of a company's cost structure during the test year and beyond, even if the costs were incurred prior to the test year.[29] The fact that issuance costs are higher or lower during different periods does not change that finding. As such, I continue to disagree with Dr. Griffing's calculation of his flotation cost adjustment.

---

27 D'Ascendis Rebuttal Testimony, at 27-28.
28 Griffing Direct Testimony, at 13.
29 D'Ascendis Rebuttal Testimony, at 30.

E. Size Adjustment

Q. WHAT IS YOUR RESPONSE TO DR. GRIFFING'S HYPOTHETICAL EXAMPLE REGARDING A COMPANY'S SIZE AND ITS CUSTOMER BASE?

A. First, although Dr. Griffing focuses solely on the relationship between a company's size and the relative size of its largest customers, he does not address the larger issue. That is, smaller companies are less equipped to handle significant events generally. As stated in my Direct Testimony:

> Size affects business risk because smaller companies generally are less able to cope with significant events that affect sales, revenues, and earnings. For example, smaller companies face more risk exposure to business cycles and economic conditions, both nationally and locally. Additionally, the loss of revenues from a few larger customers would have a greater effect on a small company than on a bigger company with a larger, more diverse, customer base.[30]

As noted above, the loss of larger companies was simply an example of the types of risks and potentially significant events that have a relatively larger effect on smaller companies.

Q. WHAT IS YOUR RESPONSE TO DR. GRIFFING'S STATEMENT THAT THE SIZE PREMIUM IS NOT PRESENT FOR INDICATORS OTHER THAN MARKET CAPITALIZATION?

A. As discussed in my Rebuttal Testimony, Duff & Phelps calculates small size risk premiums using various measures of size, including: (1) market value of common equity; (2) book value of common equity; (3) five-year

30 D'Ascendis Direct Testimony, at 66.

average net income; (4) market value of invested capital; (5) total assets; (6) five year average EBITDA; and (7) total sales.[31] As shown in Exhibit___(DWD-2), Schedule 5, the Company is smaller and has a higher level of risk than the proxy group based on all measures. Given that, I disagree with Dr. Griffing's statement that the size premium is a phenomenon only found in the study of market capitalizations.

F. Capital Structure

Q. WHY DID YOU CONSIDER THE RANGE OF COMMON EQUITY RATIOS OF THE PROXY COMPANIES IN EVALUATING THE REASONABLENESS OF THE COMPANY'S REQUESTED CAPITAL STRUCTURE?

A. I considered the range of results to ensure that the Company's capital structure was reasonable relative to the proxy companies. As discussed in my Rebuttal Testimony, because the Company's capital structure was consistent with its peers, it is reasonable to use the actual capital structure and not a hypothetical capital structure as Dr. Griffing proposes.[32]

G. Economic Conditions

Q. DO YOU AGREE WITH DR. GRIFFING THAT ECONOMIC CONDITIONS ARE REFLECTED IN THE MARKET DATA USED TO ESTIMATE THE ROE?

A. Yes, I do. It is for that reason that I did not adjust my analytical models to reflect current economic conditions. However, current conditions provide context for the analytical model results. As discussed in my

31 D'Ascendis Rebuttal Testimony, at 34-35.
32 D'Ascendis Rebuttal Testimony, at 38-40.

Rebuttal Testimony, current and expected market conditions are dynamic and point to a directionally higher ROE for natural gas distribution utilities. Specifically, the current inflationary environment is influencing monetary policy, which will put upward pressure on both interest rates and the investor-required return.[33]

The current and expected increase in the investor-required return is evidenced in the fact that both Dr. Griffing's and my analytical results have generally increased since the filing of our direct testimonies. That has been reflected in my higher recommended range (*i.e.,* 10.70% - 13.36%) and in a 14-basis point increase in Dr. Griffing's ROE recommendation.

III. RESPONSE TO AARP WITNESS MALCOLM

Q. PLEASE SUMMARIZE MR. MALCOLM'S SURREBUTTAL TESTIMONY AS IT RELATES TO THE COMPANY'S ROE.

A. Mr. Malcolm does not agree that an ROE of 10.50% is appropriate for NSP because their parent company, Xcel Energy, has received authorized returns below 10.50% in other jurisdictions. Mr. Malcolm specifically points to the recently authorized returns of 9.20% and 9.30% for PSCO's natural gas and electric operations, respectively.[34]

33 D'Ascendis Rebuttal Testimony, at 5-13.
34 Malcolm Surrebuttal Testimony, at 2.

Q. WHAT IS YOUR RESPONSE TO MR. MALCOLM?

A. The references to recently authorized returns for PSCO's natural gas and electric operations are not relevant to the ROE for NSP in this proceeding. As a preliminary matter both ROEs referenced by Mr. Malcolm were the result of settled proceedings. Settlements represent a give and take between parties. Further, the Settlement Agreement in PSCO's electric rate case (Proceeding No. 21A-0317E) states:

> Except as expressly set forth herein, nothing in this Settlement Agreement is intended to have precedential effect or bind the Settling Parties with respect to positions they may take in any other proceeding regarding any of the issues addressed in this Settlement Agreement. No Settling Party concedes the validity or correctness of any regulatory principle or methodology directly or indirectly incorporated in this Settlement Agreement. Furthermore, this Settlement Agreement does not constitute agreement, by any Settling Party, that any principle or methodology contained within or used to reach this Settlement Agreement may be applied to any situation other than the above-captioned proceeding, except as expressly set forth herein.[35]

In addition, determining the ROE is based on a point-in-time analysis that reflects current market conditions and expectations. For example, the PSCO rate cases were filed before the COVID-19 pandemic and are not representative of current and expected market conditions. Relying exclusively on authorized returns to determine the reasonableness of my recommended ROE results in a mismatch of market data and economic

---

35 Public Service Company of Colorado, *In the Matter of advice letter No. 1857 – Electric filed by Public Service Company of Colorado to revise its Colorado PUC No, 8 – Electric tariff to revise jurisdictional base rate revenues, implement new base rates for all electric rate schedules, and make other proposed tariff changes effective August 2, 2021*, Colorado Public Service Commission, Proceeding No. 21AL-0317E, Unopposed and Comprehensive Settlement Agreement, at 29.

conditions. Lastly, as noted above, Dr. Griffing and I agree that authorized returns are "not a good substitute for current, forward-looking ROE analyses."[36]

Q. DO YOU HAVE ANY FURTHER COMMENTS RELATED TO THE USE OF AUTHORIZED RETURNS IN THIS PROCEEDING?

A. The Commission should consider NSP as a stand-alone company because it is NSP's rate base to which the overall rates of return set forth in this proceeding will be applied, as noted above. To do otherwise would be discriminatory, confiscatory, and inaccurate. It is also a basic financial precept that the use of the funds invested gives rise to the risk of the investment. As Brealey and Myers state:

> The true cost of capital depends on the use to which the capital is put.
>
> ***
>
> Each project should be evaluated at its own opportunity cost of capital; the true cost of capital depends on the use to which the capital is put. **(italics and bold in original)**[37]

Morin confirms Brealey and Myers when he states:

> Financial theory clearly establishes that the cost of equity is the risk-adjusted opportunity cost of the investors and not the cost of the specific capital sources employed by the investors. The true cost of capital depends on the use to which the capital is put and not on its source. The Hope and Bluefield doctrines have made clear that the relevant considerations in calculating a company's cost of

36 Griffing Surrebuttal Testimony, at 12.

37 Richard A. Brealey and Stewart C. Myers, Principles of Corporate Finance, McGraw-Hill, Third Edition, 1988, at pp. 173, 198.

> capital are the alternatives available to investors and the returns and risks associated with those alternatives.[38]

Additionally, Levy and Sarnat state:

> The firm's cost of capital is the discount rate employed to discount the firm's average cash flow, hence obtaining the value of the firm. It is also the weighted average cost of capital, as we shall see below. The weighted average cost of capital should be employed for project evaluation… only in cases where the risk profile of the new projects is a "carbon copy" of the risk profile of the firm[39]

Although Levy and Sarnat discuss a project's cost of capital relative to a firm's cost of capital, these principles apply equally to the use of a proxy group-based cost of capital. Each company must be viewed on its own merits, regardless of the source of its equity capital. As *Bluefield* clearly states:

> A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; [40]

In other words, it is the "risks and uncertainties" surrounding the property employed for the "convenience of the public" which determines the appropriate level of rates. In this proceeding, the property employed "for

38 Roger A. Morin, Modern Regulatory Finance, PUR Books LLC, 2021, at 523.
39 Haim Levy & Marshall Sarnat, Capital Investment and Financial Decisions, Prentice/Hall International, 1986, at 465.
40 *Bluefield Water Works Improvement Co. v. Public Serv. Comm'n*, 262 U.S. 679 (1922), at 6.

the convenience of the public" is the North Dakota jurisdictional gas rate base of NSP. Thus, it is only the risk of investment in NSP that is relevant to the determination of the cost of common equity to be applied to the common equity-financed portion of that rate base. Stated differently, the ROE set in this proceeding must be based on the risks faced by the Company. The returns authorized by the Colorado Public Utilities Commission for one of Xcel Energy's other subsidiaries (i.e., PSCO) should not be solely relied upon to determine the reasonableness of my recommended ROE in this proceeding.

IV. CONCLUSION

Q. SHOULD ANY OF THE ARGUMENTS MADE BY DR. GRIFFING OR MR. MALCOLM PERSUADE THE COMMISSION TO LOWER THE RETURN ON COMMON EQUITY APPROVED FOR NSP BELOW YOUR RECOMMENDATION?

A. No, they should not. My recommended cost of common equity of 10.50%, is both reasonable and conservative. It will provide the Company with sufficient earnings to enable it to attract necessary new capital efficiently and at a reasonable cost, to the benefit of both customers and investors.

Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?

A. Yes, it does.

STATE OF NORTH DAKOTA
BEFORE THE
PUBLIC SERVICE COMMISSION

In the Matter of the Application of Northern States Power Company for Authority To Increase Rates for Natural Gas Service In North Dakota	))))	Case No. PU-21-381

AFFIDAVIT OF
Dylan D'Ascendis

I, the undersigned, being duly sworn, depose and say that the foregoing is the Surrebuttal Testimony of the undersigned, and that such Surrebuttal Testimony and the exhibits or schedules sponsored by me to the best of my knowledge, information and belief, are true, correct, accurate and complete, and I hereby adopt said testimony as if given by me in formal hearing, under oath.

____
Dylan D'Ascendis

Subscribed and sworn to before me, this 3 day of May, 2022.

Margaret A Clancy
____
Notary Public
My Commission Expires:
6/9/2024

Margaret A Clancy
Notary Public of New Jersey
My Commission Expires 6/9/2024