BEFORE THE NEW MEXICO PUBLIC REGULATION COMMISSION

IN THE MATTER OF THE APPLICATION OF PUBLIC SERVICE COMPANY OF NEW MEXICO FOR REVISION OF ITS RETAIL ELECTRIC RATES PURSUANT TO ADVICE NOTICE NO. 595	)	
	)	**Case No. 22-00270-UT**
PUBLIC SERVICE COMPANY OF NEW MEXICO,	)	
Applicant	)	

DIRECT TESTIMONY

OF

YANNICK GAGNE

December 5, 2022

NMPRC CASE NO. 22-00270-UT
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WITNESS FOR
PUBLIC SERVICE COMPANY OF NEW MEXICO

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AFFIRMATION

DIRECT TESTIMONY OF
YANNICK GAGNE
NMPRC CASE NO. 22-00270-UT

I. INTRODUCTION AND PURPOSE

Q. PLEASE STATE YOUR NAME AND POSITION.

A. My name is Yannick Gagne. I am employed by Willis Towers Watson as a Managing Director and Actuary, and am the Head of the Retirement Business for the Southeast Region.

Q. PLEASE DESCRIBE WILLIS TOWERS WATSON AND YOUR QUALIFICATIONS.

A. Willis Towers Watson is a leading provider of actuarial and retirement consulting services. We serve as the actuary for over half of the U.S. Fortune 1000 Utilities and have provided rate case support and/or testimony in most jurisdictions. We have provided support and testified in several of Public Service Company of New Mexico's ("PNM" or "Company") rate cases, including direct testimony by my colleague Gene Wickes in PNM's 2015 rate case (Case No. 15-00261-UT), and my testimony in the 2016 rate case (Case No. 16-00276-UT). Personally, I have provided actuarial and consulting services for more than 25 years, working with more than fifteen different regulated utilities. During my career, I provided rate case testimony and support for filings in New Mexico, Arizona, California, Hawaii, Missouri, Oregon, Texas, and Washington. A copy of my qualifications is included in PNM Exhibit YG – 1.

Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?

A. The purpose of my testimony in this proceeding is to provide background and additional support related to PNM's cost of service requests related to pension benefits and retiree medical benefits (also referred to as Post-Employment Benefits Other than Pensions, or "PBOP"). Specifically, I begin by providing background on the separation of Electric and Gas components of the qualified pension plan. Next, I provide background on the calculations of the projected Pension and PBOP expenses for the Test Period, which are included in PNM's cost of service request. I also provide support for continued inclusion of the prepaid pension asset in rate base, which has been approved in prior proceedings and upheld upon appeal. Finally, I provide details and justification for the appropriate adjustments to be made to the amount of cost to be included in cost of service for PBOP.

II. BACKGROUND

Q. WHAT PENSION AND PBOP PLANS ARE COVERED IN YOUR TESTIMONY?

A. My testimony covers three plans sponsored by the Company. There are two defined benefit plans (collectively referred to as "Pensions") and one retiree medical plan. These are:

1) The PNM Resources, Inc. Employee's Retirement Plan ("Qualified Pension Plan"), a qualified defined benefit plan under the Employee Retirement Income Security Act ("ERISA");

2) The PNM Resources, Inc. Non-Qualified Retirement Plan ("Non-qualified Retirement Plan"), a non-qualified defined benefit plan; and

3) The PNM Resources, Inc. Post-Retirement Healthcare Plan ("PBOP" or "Retiree Medical"), which provides for medical and dental coverage for certain retirees.

Q. HAS THE COMPANY BEEN ALLOWED TO RECOVER COSTS ASSOCIATED WITH ITS PENSION AND PBOP PLANS IN PRIOR PROCEEDINGS?

A. Yes. The following amounts have been included in rates for the Company in prior proceedings:

1) An amount equal to the annual net periodic benefit cost calculated under applicable accounting standards (Accounting Standards Codification ("ASC") Topic 715) associated with the Qualified Pension Plan, the Non-qualified Retirement Plan and the PBOP; and

2) For Pensions, a return on amounts contributed by shareholders to the Qualified Pension Plan in excess of cumulative annual pension expenses previously included in cost of service via inclusion of the prepaid pension asset in rate base.

Q. PLEASE DESCRIBE THE ACCOUNTING TREATMENT FOR PNM'S PENSION PLANS.

A. PNM accounts for its Pensions in accordance with ASC 715. ASC 715 requires the unfunded projected benefit obligation (i.e., the difference between the value of the pension plan assets and the projected benefit obligation) to be recognized as a liability on the balance sheet. Prior service costs and unrealized actuarial gains or losses are recorded to Accumulated Other Comprehensive Income and systematically recognized as an expense over subsequent periods, which PNM recovers through pension expense.

FERC Docket No. AI07-1-000 provides further guidance for accounting of defined benefit postretirement plans which allows entities to recognize regulatory assets for amounts otherwise chargeable to Accumulated Other Comprehensive Income under ASC 715 to the extent that they are recoverable in rates in future periods. Per the Final Order in NMPRC Case No. 08-00078-UT relating to PNM's sale of its gas utility assets, 58% of these costs are attributable to the electric portion of the utility and are recorded as a regulatory asset in accordance with FERC Docket No. AI07-1-000 and ASC 980-25. The remaining 42% of these costs are considered related to the divested gas portion of the utility and thus are recorded in Accumulated Other Comprehensive Income. In Case No. 15-00261-UT, the Commission allowed PNM to pursue annuitization of 42% of the pension obligation related to divested gas operations ("Gas Liability"). Consistent with this decision, the pension obligation and associated pension assets were effectively separated on January 1, 2018, to enable the Company to dispose of the Gas Liability over time, as authorized. Therefore, the electric portion of the pension plan is now tracked and accounted for by itself, and the 58% / 42% cost allocation is no longer necessary. Unless otherwise noted, any further reference to "pension plan" refers to the electric portion only.

Q. HOW ARE THE NET PERIODIC BENEFIT COSTS CALCULATED?

A. Under ASC 715, periodic benefit costs are made of several components including: (1) the value of benefits that employees will earn during the current year (Service Cost), (2) increases in the present value of the benefits that plan participants have earned in previous years due to interest (Interest Cost), (3) a reduction for investment earnings on plan assets that are expected to be earned during the year (Expected Return on Assets), (4) recognition of costs (or credit) from experience that differs from the assumptions, such as demographic experience and investment earnings different than assumed (amortization of Unrecognized Gains and Losses), and (5) recognition of the cost of benefit changes the plan sponsor provides for service the employees have already performed (amortization of Unrecognized Prior Service Cost).

Q. WHAT IS THE BASIS FOR DETERMINING THE AMOUNT OF NET PERIODIC BENEFIT COSTS TO BE INCLUDED IN THE REVENUE REQUIREMENTS RELATED TO THE PENSION AND PBOP PLANS IN THIS RATE CASE?

A. The amount included in revenue requirements for Pensions and PBOP is based on the projected net periodic benefit costs for the Test Period. Willis Towers Watson has prepared those projections and the results are presented below. To calculate the projected Test Period net periodic benefit costs, we first projected assets, liabilities, benefit payments, and PNM contributions for each of the three plans. We then used this information to calculate the projected net periodic benefit cost for the Test Period. Two key economic assumptions are needed for this projection: discount rate and assumed asset returns.

Projections were based on the following:

- Most recent completed actuarial valuations (January 1, 2022)
- Asset values as of June 30, 2022 (the most recent quarter end at the time projections were prepared)
- Discount rate based on current economic environment at June 30, 2022 (point in time consistent with asset values)

Please see PNM Exhibit YG-2 for the results of this analysis. The results for each plan are presented and discussed in each plan's section below.

Q. WHAT IS THE BASIS FOR DETERMINING THE DISCOUNT RATE ASSUMPTION?

A. The discount rate is the rate used to discount projected benefit payments under the plan to the valuation date. Discount rates were selected using the same methodology used in the two prior PNM rate cases, which is the same methodology used by the Company for its corporate financial statements. The discount rate assumption for each plan is determined by creating a hypothetical portfolio of high-quality corporate bonds in which cash flows (coupons and maturities) match the projected benefit payments from the plan. The effective interest rate of the resulting portfolio (interest rate at which discounted coupons and maturities equal the market price of the underlying bonds) is the discount rate. While several different methodologies may be acceptable (such as applying the plan's projected benefit payments to a yield curve), accounting standards require that the discount rate methodology be applied consistently year-after-year, unless the plan's circumstances have materially changed so that the methodology no longer represents management's best estimate.

Q. WHAT IS THE BASIS FOR DETERMINING THE EXPECTED RETURN ON ASSET ASSUMPTION?

A. The expected return on asset assumption is used in the net periodic benefit cost calculation. The net periodic cost is reduced by the investment returns expected to be generated by the plan assets, calculated based on this assumption. The expected return on asset assumption is based on the same methodology used in prior rate cases, which is the same methodology used by the Company for its corporate financial statements. It is derived from three components:

a) An expected return resulting from plan assets invested passively in the various asset classes (like index funds, for example a fund that matches returns of the S&P 500), based on the plan's target asset allocation, plus

b) An additional return resulting from active management of the assets, net of manager expenses paid by the plan (also known as manager alpha), minus

c) An adjustment for administrative expenses paid from trust assets. For purposes of this projection administrative expenses and manager alpha were assumed to be equal.

III. QUALIFIED PENSION PLAN

Q. WERE ANY ADJUSTMENTS MADE TO REFLECT THAT IN CASE NO. 15-00261-UT, THE COMMISSION ALLOWED PNM TO PURSUE ANNUITIZATION OF 42% OF THE PENSION OBLIGATION, WHICH IS THE LIABILITY ASSOCIATED WITH THE DIVESTED GAS OPERATIONS?

A. Yes. Effective January 1, 2018, assets and liabilities were effectively separated between the "Electric Plan" and "Gas Plan" based on the 58%/42% allocation. Participants were allocated among the two plans, a step that is necessary to execute the annuitization of the Gas Liability in due time. Participants were allocated to the Gas Plan until the resulting Gas liability equaled or exceeded 42% of the total liability (ensuring that the Electric Plan would receive no more than 58% of the total obligation). Plan assets were also allocated, so that the Electric Plan received 58% of total plan assets. Since the split, the Electric Plan assets and liabilities have been tracked and reported separately.

Q. ARE THERE OTHER COMPONENTS USED IN DEVELOPING THE NET PERIODIC BENEFIT COST THAT SHOULD ALSO BE ALLOCATED?

A. Yes. There are two other main components beyond assets and liabilities. Those are prior service cost and unrecognized losses.

Q. HOW WAS THE PRIOR SERVICE COST ALLOCATED?

A. At January 1, 2018, the prior service cost balance was a credit of $2,485,184. Because this is a credit, its effect is to reduce net periodic benefit costs in future periods. The full prior service credit was allocated to the Electric Plan, meaning the Electric Plan receives the full benefit via reduction of future net periodic benefit cost. The reason is that the plan change that resulted in the prior service credit only affected active employees, and occurred after the divestiture of the gas operations. Therefore, it is reasonable to assume that the entire benefit is related to electric operations.

Q. HOW WAS THE UNRECOGNIZED LOSS ALLOCATED?

A. The unrecognized loss was allocated using the 58%/42% allocation between the Electric Plan and the Gas Plan as of January 1, 2018.

Q. HOW HAS THE FUNDED STATUS OF THE ELECTRIC PLAN CHANGED SINCE THE MOST RECENT RATE REQUEST?

A. In my testimony in Case No. 16-00276-UT, I noted that the Electric Plan had an unfunded liability of about $23 million as of December 31, 2015 (58% of the $40 million unfunded Projected Benefit Obligation for the total plan), the most recent formal measurement date. Since that time, the funded status has steadily improved, with the unfunded liability for the Electric Plan reduced to $3.8 million as of December 31, 2021, the most recent formal measurement date, a funded percentage of 98.9%.

Q. WHAT CAUSED THE IMPROVEMENT IN THE FUNDED STATUS?

A. The funded status improvement can be primarily attributed to positive investment experience, as actual investment returns have exceeded expectations during this period.

Q. HOW HAVE INTEREST RATES IMPACTED THE FUNDED STATUS?

A. Through December 31, 2021, interest rates have dropped by approximately 100 basis points since the prior rate filing. While this decrease in rates caused the liabilities to increase, PNM employed a rate-hedging investment strategy which caused the increase in liabilities to be mostly offset by an increase in the trust assets, protecting the funded status of the plan.

Q. HOW HAVE THE MARKET MOVEMENTS IN THE FIRST HALF OF 2022 IMPACTED THE FUNDED STATUS?

A. During the first half of 2022, interest rates increased by around 200 basis points and equity markets had significant losses. As a result, during this period all major asset categories, from equities to fixed income, lost significant value (for example, the

S&P 500 index was down nearly 20% in that period). However, the investment strategy employed by PNM provided significant funded status protection. The estimated funded percentage as of June 30, 2022, was 92.8%, a reduction in funded percentage of 6.1% despite much more significant losses in capital markets.

Q. HOW ARE CASH CONTRIBUTIONS TO THE PENSION PLAN DETERMINED?

A. The funding of a pension plan is determined based upon prudent business practices within the following legal constraints of ERISA, as modified by the Pension Protection Act ("PPA"), and the Internal Revenue Code ("IRC"):

- The minimum required annual contribution,
- The maximum contribution which can be deducted for tax purposes, and
- The fiduciary responsibility to prudently protect the interests of the plan participants and beneficiaries.

The minimum and maximum funding rules set forth under ERISA, the PPA, and the IRC use accrual methodologies, but they are different from the methodology used under ASC 715 which is an accounting standard. Over the long run, the cumulative employer cash contributions made to a plan and the cumulative annual pension cost amounts should be equal. But in the short and intermediate term, there can be significant differences.

It is important to note that the minimum required contribution is the minimum standard by which plans must contribute to avoid violating the law. The minimum required contribution is not an amount that sufficiently funds the plan to the level needed to settle all plan obligations. In no way is such a minimum contribution to be interpreted as the appropriate or prudent funding policy. In fact, many plan sponsors contribute amounts beyond the minimum required contribution.

Q. ARE ANY COMPANY CASH CONTRIBUTIONS FORECASTED BETWEEN JUNE 30, 2022, AND DECEMBER 31, 2024?

A. No. While at December 31, 2021 (the last formal measurement date for PNM's financial statements), the pension plan shows an unfunded Projected Benefit Obligation ("PBO") of about $3.8 million, no contributions are projected though the end of the period January 1, 2024 to December 31, 2024 (the Test Period). This is the result of several changes to minimum funding rules enacted by Congress, which resulted in a reduction in minimum required contributions for qualified pension plans. As a result, the current funding balances are projected to be sufficient to satisfy all minimum funding requirements through the Test Period.

Q. WHAT IS THE PROJECTED NET PERIODIC BENEFIT COST FOR THE QUALIFIED PENSION PLAN FOR THE TEST PERIOD?

A. The net periodic benefit cost for the qualified pension plan is projected to be $3,970,528 for the Test Period (January 1, 2024, to December 31, 2024) compared to $4,794,940 for the previous Test Period (2018). The decrease in cost is mainly due to smaller assets and liabilities resulting from pension benefits being paid out to participants in combination with the effect of the increase in discount rate and asset gains since the prior measurement. PNM Exhibit YG-2 shows more details about these amounts.

Q. HOW IS THE PROJECTED NET PERIODIC BENEFIT COST FOR THE QUALIFIED PENSION PLAN EXPECTED TO CHANGE BEYOND THE TEST PERIOD?

A. Our most recent projections of the new periodic benefit cost for the pension plan shows expected annual increases in costs through 2027, with the annual cost increasing from $4.0 million in 2024 (the Test Period) to $9.7 million in 2027. The reasons for the change include decreasing assets as benefits are paid, the recognition of asset losses occurring during the first half of 2022 in the Market Related Value of Assets and the amortization of historical losses, by which the Prepaid Pension Asset will be written down. PNM Exhibit YG-3 shows more details about these amounts.

Q. ARE THESE COSTS NECESSARY AND REASONABLE COSTS FOR PROVIDING PENSION BENEFITS TO EMPLOYEES?

A. Yes. In a defined benefit plan, the Company promises to make pension payments for the employees' lifetime. Therefore, the actual cost for providing those benefits will not be known until all promised payments have been made. The net periodic benefit cost provides an objective and systematic way to recognize those costs over time. These costs are therefore necessary to fulfill the benefits promised to employees and former employees.

Q. IS PNM ALSO SEEKING TO INCLUDE IN RATE BASE AN AMOUNT RELATED TO ITS PREPAID PENSION ASSET?

A. Yes. As addressed by PNM witness Peters, PNM seeks to include an amount in rate base to reflect the prepaid pension asset. The prepaid pension asset represents the amounts contributed to the pension plan in excess of the amounts recovered in rates (the expense). In its Final Order in Case No. 15-00261-UT, the Commission reaffirmed that PNM is allowed to receive a return on the prepaid pension asset. This decision was also upheld by the New Mexico Supreme Court upon appeal. Both decisions have also confirmed that sufficient evidence was provided to support that the prepaid pension asset in the case (as of December 31, 2015) does indeed result from shareholder funded contributions.

It is important to point out that the full prepaid pension asset is used to satisfy the obligations of the plan; as such, technically PNM could ask to include the full prepaid pension asset in rate base. However, PNM limits the amount to be included in rate base to offset the reduction in pension expense resulting from those additional contributions.

Q. PLEASE EXPLAIN HOW ADDITIONAL CONTRIBUTIONS AFFECT PENSION EXPENSE.

A. As mentioned previously, one of the components of pension expense is the Expected Return on Asset. The pension expense is *reduced* by the investment returns expected to be earned on the plan assets. Therefore, each dollar of additional contribution will reduce the pension expense – and consequently the amount charged to ratepayers – by an amount equal to the expected return on such additional contributions. At December 31, 2023, projected assets used in calculating the projected Test Period expense include adjusted prepaid pension assets (or additional contributions) of $154.4 million. If the additional contributions were not made, the pension expense for the Test Period would be $9.1 million higher using the 5.90% expected return on assets assumption ($154.4 million x 5.90%). Including the adjusted prepaid pension asset in rate base neutralizes the impact of accelerated funding so that the total cost to ratepayers is the same (no more, no less) than it would have been absent the additional contributions.

Q. ARE THERE BENEFITS TO ACCELERATED FUNDING?

A. Yes. Once amounts are contributed to the pension trusts, they are invested and earn returns. Each dollar of return reduces future contributions that will be needed to satisfy plan obligations. In addition to the returns generated on invested assets, additional funding reduces the amount of variable premium the plan must pay to the Pension Benefits Guarantee Corporation (“PBGC”). Since 2008, the PNM pension plan has been subject to variable premiums every year.

Q. WHAT IS THE PBGC?

A. The PBGC is a federal agency established by Congress as part of ERISA to protect pension benefits under private sector defined benefit pension plans. If a pension plan is terminated without sufficient funds to pay all benefits, the PBGC will pay employees the benefits promised under the plan, up to certain limits set by law. The funding for the PBGC comes from premiums charged to pension plans as well as returns on assets held by the PBGC.

Q. WHAT TYPES OF PREMIUMS DOES THE PBGC CHARGE?

A. The PBGC charges two types of premiums: (1) a per participant premium charged to all single employer defined benefit plans, and (2) a variable premium charged to underfunded plans.

Q. HOW MUCH IS THE PBGC VARIABLE PREMIUM?

A. For 2022, the PBGC variable premium is 4.8% of any unfunded liability (subject to a per participant maximum). For this purpose, the liability is measured based on assumptions set by the PBGC. This liability measure is often different from the PBO used for pension cost purposes under ASC 715 and is currently much higher than the funding liability used for minimum required contribution purposes. Therefore, accelerated contributions are providing a significant additional financial benefit.

Q. IS IT YOUR UNDERSTANDING THAT THE COMMISSION HAS ALLOWED UTILITIES TO RECOVER AND EARN A RETURN ON THEIR PREPAID PENSION ASSETS?

A. Yes. Including the prepaid pension asset in rate base is consistent with past treatment approved by the Commission in previous cases, including the 2007, 2008, 2010, 2015 and 2016 PNM rate cases. In addition, this issue has been litigated before the New Mexico Supreme Court in Southwestern Public Service Company's 2012 Rate Case No. 12-00250-UT, and more recently in PNM's 2015 Rate Case No. 15-00261-UT. In both instances, the Court upheld the decision to include prepaid pension asset in rate base. *See New Mexico Atty. Gen. v. N.M. Public Regulation Comm'n*, 2015-NMSC-032, 359 P.3d 133; *Public Service Co. of N.M. v. N.M. Public Regulation Comm'n*, 2019-NMSC-012 ¶¶ 105-112, 444 P.3d 460. Given the strong precedents and the validation from the New Mexico Supreme Court, there should be no question about the appropriateness of including the prepaid pension asset in rate base.

IV. NON-QUALIFIED RETIREMENT PLAN

Q. WHAT IS THE PNM NON-QUALIFIED RETIREMENT PLAN?

A. The Non-qualified Retirement Plan is an unfunded arrangement that provides benefits to certain executives. It provides for benefits that cannot otherwise be provided under the qualified pension plan because of IRS limitations on both the amount of compensation that can be reflected and the overall benefit that can be provided.

Q. HOW ARE CONTRIBUTIONS TO THE NON-QUALIFIED RETIREMENT PLAN DETERMINED?

A. The Non-qualified Retirement Plan is unfunded; PNM contributes an amount equal to the benefits as they are paid from the plan.

Q. WHAT ARE PROJECTED CONTRIBUTIONS FOR THE JUNE 30, 2022 – DECEMBER 31, 2024 PERIOD?

A. Projected contributions to the Non-qualified Retirement Plan (equal to projected benefit payments) are as follows:

June 30, 2022 – December 31, 2022:	$643,834
2023:	$1,250,932
2024:	$1,207,509

Q. WHAT IS THE PROJECTED NET PERIODIC BENEFIT COST FOR THE NON-QUALIFIED RETIREMENT PLAN FOR THE TEST PERIOD?

A. The net periodic benefit cost for the Non-qualified Retirement Plan is projected to be $649,106 in the Test Period (January 1, 2024 to December 31, 2024). It compares to $1,031,783 for last Test Period (2018). The decrease is primarily due to a reduction in liabilities from benefits under the plan being paid to participants. PNM Exhibit YG-2 shows these amounts.

Q. ARE THESE COSTS NECESSARY AND REASONABLE COSTS FOR PROVIDING NON-QUALIFIED PENSION BENEFITS?

A. Yes. Like for the qualified pension plan, the Company promises to make pension payments for the employees' lifetime. The actual cost for providing these benefits will not be known until all promised payments have been made. The net periodic benefit cost provides an objective and systematic way to recognize those costs over time. These costs are therefore necessary to fulfill the benefits promised to employees and former employees.

Q. PNM IS PROPOSING A RATE BASE ADJUSTMENT FOR THE NON-QUALIFIED RETIREMENT PLAN. PLEASE EXPLAIN.

A. Because the Non-qualified Retirement Plan is unfunded, PNM cannot contribute amounts in excess of the benefit payments directly made to plan participants. As a result, it is not always possible for PNM to contribute the entire amount recovered. Because of this, contributions made to the Non-qualified Retirement Plan (by way of benefit payments) have been less than the amounts recovered. This is the opposite of the prepaid pension asset for the Qualified Pension Plan. In order to apply a consistent treatment, the amount of under-contributions will be subtracted from rate base.

V. PBOP (RETIREE MEDICAL) PLAN

Q. WHAT IS THE PROJECTED NET PERIODIC BENEFIT COST FOR THE PBOP PLAN FOR THE TEST PERIOD?

A. The net periodic benefit cost/(income) for the PBOP plan is projected to be ($1,751,534) for the Test Period (January 1, 2024 to December 31, 2024). This compares to $2,093,472 for the prior Test Period (2018). The decrease in cost can be attributed mainly to the increase in discount rate, and positive health care cost experience, as premiums for those benefits are lower than previously projected. PNM Exhibit YG-2 shows these amounts.

Q. ARE THESE COSTS NECESSARY AND REASONABLE COSTS FOR PROVIDING PBOP BENEFITS?

A. Yes. As with the pensions, the Company promises to provide these benefits over the employees' lifetimes. The actual cost for providing these benefits will not be known until all promised payments have been made. The net periodic benefit cost provides an objective and systematic way to recognize those costs over time. These costs are therefore necessary to fulfill the benefits promised to employees and former employees.

Q. WHAT CAUSES THE NET PERIODIC BENEFIT COST TO BE NEGATIVE (AN INCOME)?

A. As stated previously, under ASC 715, periodic benefit costs consist of several components, one of which is a reduction for expected investment earnings on plan assets during the year (Expected Return on Assets). In this case, the net benefit cost is negative (an income) because the Expected Return on Assets is greater than the sum of all other components of the benefit cost.

Q. HOW ARE THE PBOP BENEFITS FUNDED?

A. Prior to 1993, PBOP benefits were paid directly from company assets on a pay-as-you-go basis. Beginning in 1993, the company has funded PBOP benefits through contributions to trusts set aside to pay PBOP benefits.

Q. CAN PBOP ASSETS, OR RETURNS ON THOSE ASSETS, BE ACCESSED BY PNM FOR ANY PURPOSE OTHER THAN TO PAY FOR BENEFITS?

A. No. Funds within the PBOP trusts, including historical and future returns, may only be used to provide the promised retiree medical benefits to retirees until all benefits have been paid. The Company is unable to access these funds for other purposes.

Q. WHAT ADJUSTMENT SHOULD BE MADE TO THE AMOUNT INCLUDED IN COST OF SERVICE FOR PBOP?

A. Because the negative cost (income) is attributable to investment earnings that must remain in the trusts, the amount included in cost of service is set at $0. Reducing cost of service to reflect the negative PBOP cost would require PNM to pull those returns from the trusts in order to offset other costs, which PNM cannot legally do. Because the investment returns remain in the PBOP trusts and cannot be used for other purposes, customers retain the benefit. Applying a negative adjustment to cost of service would result in a “double benefit” to customers as they would benefit from a rate reduction and benefit again from the same amount being available to pay for benefits.

Q. BEYOND PAYING FOR PLAN BENEFITS, ARE THERE OTHER BENEFITS TO CUSTOMERS FROM THOSE EARNINGS REMAINING IN THE TRUSTS?

A. Yes. By remaining in the trusts, those earnings add to the plan asset balance. Future net periodic benefit costs will be reduced by the expected return on those assets, further reducing future costs to customers.

Q. HOW MUCH ASSETS ARE IN THE TRUSTS THAT IS GENERATING THE EXPECTED RETURN ON ASSETS?

A. Total PBOP trust assets as of June 30, 2022, were $74.2 million.

Q. WHAT IS THE SOURCE OF THESE ASSETS?

A. As noted earlier, beginning in 1993, the company began funding the PBOP trusts. Shareholder funds were initially used to seed the trusts with later contributions funded by both customers and shareholders. These contributions combined with the historical returns on plan assets are the source of current trust assets. However, as illustrated in PNM Exhibit YG-4, if contributions had been limited to the amounts collected in rates, and shareholder funds were not used, the trust assets would be completely depleted.

Q. HAS PNM RECEIVED A BENEFIT FOR THE ADDITIONAL COMPANY CONTRIBUTIONS?

A. No. While it could have requested so, PNM has never requested for these amounts to be included in rate base. Customers have always received the benefit of the excess contributions through a reduction in net periodic benefit cost equal to the expected return on those assets. As shown in PNM Exhibit YG-4, the sum of the difference in benefit cost for all years since 1993 due to the additional contributions is $95.7 million.

Q. WHAT WOULD THE TEST PERIOD BENEFIT COST BE IF TRUST ASSETS WERE DEPLETED IN THE MANNER DESCRIBED?

A. If there were no trust assets to generate an expected return, the net periodic benefit cost/(income) for the PBOP plan would be projected to be $2,410,958 for the Test Period (January 1, 2024 to December 31, 2024). This represents the components of the benefit cost excluding the Expected Return on Assets.

Q. ARE YOU RECOMMENDING THAT THIS ALTERNATIVE BENEFIT COST AMOUNT CALCULATED WITHOUT ANY EXPECTED RETURN ON ASSETS BE INCLUDED IN COST OF SERVICE?

A. No. As discussed above, while it might be reasonable to request the full benefit cost assuming no Expected Return on Assets, we are only recommending that the amount to be included in cost of service be limited to a floor of zero because the trust assets cannot be used for other purposes than to pay PBOP benefits.

Q. HOW WILL CONTRIBUTIONS TO THE PBOP TRUSTS BE IMPACTED UPON THE EFFECTIVE DATE OF THE NEW RATES?

A. PNM is required to contribute to the PBOP trusts any amounts recovered for PBOP and not used to directly pay benefits. With PBOP recovery set to zero, there will be no expected contributions to the trusts. However, PNM will continue to make contributions to directly pay benefits that are not eligible for payment from a trust.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes.

GCG#530058

Resume of Yannick Gagne

PNM Exhibit YG-1

Is contained in the following 1 page.

**DIRECT TESTIMONY OF
YANNICK GAGNE
NMPRC CASE NO. 22-00270-UT**

**PNM Exhibit YG-1
Statement of Qualifications for
Yannick Gagne**

Current Responsibilities and Experience:

I have over 25 years of experience consulting with organizations on the design and financial considerations of their pension programs. I am currently employed by Willis Towers Watson as a Managing Director and Actuary.

Education:

Bachelor of Science – Actuarial Science
Laval University, Canada

Employment:

Willis Towers Watson (formerly Towers Watson & Company)
Senior Consultant and Actuary
Head of Retirement Business – Southeast Region

Aon Hewitt
Principal
San Francisco, Pacific Northwest and Hawaii Retirement Practice Leader

Professional Organization:

Fellow of the Society of Actuaries
Enrolled Actuary under the Employee Retirement Income Security Act of 1974 (“ERISA”)

Retirement Consulting and Utility Experience:

During my more than 25 years of retirement consulting experience, I have helped senior human resources and finance executives determine how to manage and configure retirement programs that best support organizational objectives.

In addition to working with many large corporate organizations, I have worked with more than fifteen regulated utilities providing actuarial and retirement consulting services. In that role, I provided testimony support in rate case proceedings, as well as retirement program design and union negotiation support.

Specifically regarding rate case support, I provided support for various rate case filings in New Mexico, Arizona, California, Hawaii, Missouri, Oregon, Texas, and Washington (direct testimony in New Mexico, California, Hawaii, and Texas).

Estimated Pension and Retiree Medical Expenses for the January 1, 2024 to December 31, 2024 Period ("Test Period") memo

PNM Exhibit YG-2

Is contained in the following 5 pages.

Willis Towers Watson

Memo

Date: August 30, 2022

To: Ed Jeung, *PNM Resources, Inc.*

From: Yannick Gagne, FSA & Brian Arnell, FSA, *Willis Towers Watson*

Subject: **Estimated FY2024 Pension and Retiree Medical Expense**

PNM Resources, Inc. (PNM) has requested that Willis Towers Watson provide estimated pension and retiree medical expense for the PNM Resources, Inc. Employees' Retirement Plan (PNM Pension), PNM Resources, Inc. Post-Retirement Healthcare Plan (PNM Retiree Medical), and PNM Resources, Inc. Non-Qualified Retirement Plan (PNM Non-Qualified) for FY2024, the "Test Year". The results of our analysis are below. For comparison, we are also showing estimated FY2018 expenses which were included in the prior rate case.

Plan	Estimated FY2018 Expense "Test Year"	Estimated FY2024 Expense "Test Year"
PNM Pension (Electric)	$4,794,940[1]	$3,970,528
PNM Retiree Medical	$2,093,472	($1,741,534)[2]
PNM Non-Qualified	$1,031,783	$649,106

The tables on the next pages reflect the key components of these expense figures, explanation of the major factors for any changes since the prior test year, as well as the underlying data and assumptions for each plan.

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[1] Reflect 58% allocation of full PNM Pension cost (before January 1, 2018 separation) to Electric business

[2] Negative expense is an income due to expected asset returns in excess of other costs. Note, however, that these funds 1) are attributable to historical shareholder contributions and 2) cannot be legally accessed or removed from the trusts until all benefits have been paid.

PNM Pension (Electric)

	Estimated FY2018 Expense "Test Year" [3]	Estimated FY2024 Expense "Test Year"	Explanation
Service Cost	$0	$0	
Interest Cost	$13,953,517	$12,861,806	Decrease due to smaller obligation (see below)
Expected Return on Assets	($18,007,065)	($15,741,783)	Increase due to lower asset values (see below)
Prior Service Cost Amortization	($559,865)	$0	Fully amortized in 2020
Gain/Loss Amortization	$9,408,353	$6,850,505	Decrease primarily due to gains from the increase in discount rate and historical asset gains with deferral of recent asset losses
Total Expense	**$4,794,940**	**$3,970,528**	
Projected Benefit Obligation	$360,320,089	$269,051,777	Reduction due to benefit payments, offset by the lower discount rate
Fair Value of Assets	$309,553,122	$239,571,374	Reduction due to benefit payments and asset losses in 2022
Market Related Value of Assets	$313,873,205	$278,600,029	Exceeds Fair Value of Assets due to deferral of losses during first half of 2022
Assumptions and Data			
Discount Rate	4.03%	5.00%	
Expected Return on Assets	6.00%	5.90%	
Census Date	1/1/2016	1/1/2022	

[3] Reflect 58% allocation of full PNM Pension cost (before January 1, 2018 separation) to Electric business

PNM Retiree Medical

	Estimated FY2018 Expense "Test Year"	Estimated FY2024 Expense "Test Year"	Comments
Service Cost	$107,049	$0	No further benefits accruing
Interest Cost	$3,783,792	$2,410,958	Decrease due to smaller obligation (see below)
Expected Return on Assets	($4,516,653)	($4,152,492)	
Prior Service Cost Amortization	($1,513,393)	$0	Fully amortized in 2019
Gain/Loss Amortization	$4,232,677	$0	Decrease due primarily to experience gains from lower health care costs and higher interest rates
Total Expense	**$2,093,472**	**($1,741,534)**	
Accumulated Projected Benefit Obligation	$98,989,955	$51,113,462	Gains from lower health care costs and higher discount rate and benefits paid out
Fair Value of Assets	$71,775,343	$73,527,153	
Market Related Value of Assets	$72,045,935	$86,047,494	Exceeds Fair Value of Assets due to deferral of losses during first half of 2022
Assumptions and Data			
Discount Rate	3.97%	5.00%	
Expected Return on Assets	6.50%	4.90%	
Census Date	1/1/2016	1/1/2022	

PNM Non-Qualified

	Estimated FY2018 Expense "Test Year"	Estimated FY2024 Expense "Test Year"	Comments
Service Cost	$0	$0	
Interest Cost	$616,064	$457,005	Decrease due to smaller obligation (see below)
Expected Return on Assets	$0	$0	
Prior Service Cost Amortization	$0	$0	
Gain/Loss Amortization	$415,719	$192,101	Decrease due to amounts previously recognized
Total Expense	**$1,031,783**	**$649,106**	
Projected Benefit Obligation	$16,991,016	$9,736,507	Reduction as benefits are paid out and higher discount rate
Fair Value of Assets	$0	$0	
Market Related Value of Assets	$0	$0	
Assumptions and Data			
Discount Rate	3.79%	5.00%	
Expected Return on Assets	N/A	N/A	
Census Date	1/1/2016	1/1/2022	

Additional Calculation Details

Assets were projected from asset values as of June 30, 2022 assuming no return through year-end 2022 and actual returns equal to the expected return on asset assumption for 2023. No contributions were assumed for the PNM Electric pension plan. 55% of retiree medical benefits are assumed to be paid from corporate assets.

June 30, 2022 assets for funded plans were as follows:

Plan	Trust Assets as of June 30, 2022
PNM Pension (Electric)	$268,508,452
PNM Retiree Medical	$74,245,862

Retirement expectations were adjusted to account for the San Juan Generating Station closure in late 2022.

Except as otherwise provided herein, the FY2018 "Test Year" results presented above are based on the data, assumptions, methods, plan provisions and other information, outlined in the Estimated 2017-2018 Expense Memo dated September 8, 2016.

Except as otherwise provided herein, the FY2024 "Test Year" results presented above are based on the data, assumptions, methods, plan provisions and other information, outlined in the actuarial valuation reports to determine benefit cost for the plans for the fiscal year beginning January 1, 2022 dated March 14, 2022.

Therefore, such information, and the reliances and limitations of the valuation reports and their use, should be considered part of this exhibit. The consulting actuaries above are members of the Society of Actuaries and meet the "Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States" relating to pension and postretirement welfare plans. Our objectivity is not impaired by any relationship between the plan sponsor and our employer, Willis Towers Watson.

PNM Pension (Electric) – Expense Projection

PNM Exhibit YG-3

Is contained in the following 1 page.

PNM Pension (Electric) - Expense Projection

	2023	**2024**	**2025**	**2026**	**2027**
Service Cost	-	-	-	-	-
Interest Cost	13,404,932	12,861,806	12,312,147	11,760,941	11,209,404
Expected Return on Assets	(16,641,412)	(15,741,783)	(14,535,861)	(12,918,735)	(11,290,716)
Prior Service Cost Amortization	-	-	-	-	-
Gain/Loss Amortization	6,423,355	6,850,505	7,608,937	8,727,666	9,797,888
Total Expense	**3,186,875**	**3,970,528**	**5,385,223**	**7,569,872**	**9,716,576**

Projected Benefit Obligation (as of beginning of year)	280,195,830	269,051,777	257,933,684	246,518,442	235,343,194
Fair Value of Assets (as of beginning of year)	251,509,399	239,571,374	227,503,519	214,970,577	202,499,095
Market Related Value of Assets	294,128,894	278,600,029	258,036,014	230,236,825	202,499,095

Benefit Payments	24,493,123	23,923,116	23,670,177	22,878,303	22,585,730
Contributions	-	-	-	-	-

Assumptions

Discount Rate	5.00%	5.00%	5.00%	5.00%	5.00%
Expected Return on Assets	5.90%	5.90%	5.90%	5.90%	5.90%

Except as otherwise provided herein, the results presented above are based on the data, assumptions, methods, plan provisions and other information, outlined in the Estimated 2024 Expense Memo dated August 30, 2022. Therefore, such information, and the reliances and limitations of the valuation reports and their use, should be considered part of this exhibit.

Report on the Impact of the Pattern of PNM’s ASC 715 Contributions

PNM Exhibit YG-4

Is contained in the following 12 pages.

Willis Towers Watson

PNM Resources, Inc. Post-Retirement Healthcare Plan

Report on the Impact of the **Pattern of PNM's ASC 715** Contributions

October 2022

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Purpose and actuarial statement

This report documents the results of a study on the impact of PNM's ASC 715 contributions, performed by Willis Towers Watson US LLC ("Willis Towers Watson") for Public Service Company of New Mexico (PNM) as originally required in the Final Order under Case No. 07-00077-UT.

The information contained in this report was prepared for the internal use of PNM Resources, Inc. and its auditors. It is not intended for and may not be used for other purposes, and we accept no responsibility or liability in this regard. PNM Resources, Inc. may distribute this actuarial valuation report to the appropriate authorities who have the legal right to require PNM Resources, Inc. to provide them this report, in which case PNM Resources, Inc. will use best efforts to notify Willis Towers Watson in advance of this distribution. Further distribution to, or use by, other parties of all or part of this report is expressly prohibited without Willis Towers Watson's prior written consent. Willis Towers Watson accepts no responsibility for any consequences arising from any other party relying on this report or any advice relating to its contents.

This report is provided subject to the terms set out herein and in our engagement letter dated May 5, 2021 and any accompanying or referenced terms and conditions. This report is provided solely for PNM Resources, Inc.'s use and for the specific purposes indicated above. It may not be suitable for use in any other context or for any other purpose.

In preparing these results, we have relied upon information and data provided to us orally and in writing by PNM Resources, Inc. and other persons or organizations designated by PNM Resources, Inc. We have relied on all the data and information provided, including plan provisions, membership data and asset information, as being complete and accurate. We have not independently verified the accuracy or completeness of the data or information provided, but we have performed limited checks for consistency.

The results summarized in this report involve actuarial calculations that require assumptions about future events. PNM Resources, Inc. is responsible for the selection of the assumptions. We believe that the assumptions used in this report are reasonable for the purposes for which they have been used.

In our opinion, all calculations are in accordance with FASB Accounting Standards Codification Topic 715-60 (formerly known as FAS 106) and the procedures followed and the results presented are in conformity with applicable actuarial standards of practice. References in this report to specific financial accounting standards such as those named in this paragraph are intended to encompass standards that supersede the referenced statements under the FASB Accounting Standards Codification.

The undersigned consulting actuaries are members of the Society of Actuaries and meet the "Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States" relating to pension plans. Our objectivity is not impaired by any relationship between PNM Resources, Inc. and our employer, Willis Towers Watson US LLC.

Yannick Gagne, FSA
Managing Director, Retirement
October 19, 2022

Brian M. Arnell, FSA
Director, Retirement
October 19, 2022

Willis Towers Watson US LLC

https://wtwonline.sharepoint.com/sites/tctclient_606112_2022RETANN/Documents/2022 PNMMED Report on pattern of ASC 715 Contributionse.docx

Report on the Impact of the Pattern of PNM's ASC 715 Contributions

Beginning with Case No. 2567, PNM was required to make quarterly contributions to build trust assets to cover its liabilities under ASC 715 according to the following annual pattern:

Table 1 ($ thousands)	
Year	Annual Amount
1995	$4,122
1996	4,122
1997	5,645
1998	6,152
1999	6,152
2000	6,152
2001	6,152
2002	5,487
2003	5,265
2004	5,265
2005	5,265
2006	5,265
2007	5,581
2008	4,748
2009	2,547
2010	2,547
2011	2,841
2012	3,253
2013	3,253
2014	3,253
2015	3,253
2016	2,440
2017	0
2018[1]	0
2019	0
2020	0
2021	0
2022	0
2023	0

[1] Beginning in February 2018, the amount recovered is first used to offset prior excess contributions.

The Orders also required that PNM make the contributions on a tax effective basis. To maximize the tax effective funding of its ASC 715 liabilities PNM took two critical steps: it began funding earlier than 1995 (funding began in 1993), and in some years it paid part of its contributions directly to participants as benefits payments instead of making the contributions to a trust and immediately taking them back out of the trusts to make the benefit payments.

Using these steps, PNM's actual funding has been as follows:

Table 2 ($ thousands)			
Year	Funding Pattern under Rate Cases	Actual PNM ASC715 Funding	Cumulative Excess Funding
1993	$0	$2,096	$2,096
1994	0	6,516	8,612
1995	4,122	5,533	10,023
1996	4,122	5,527	11,428
1997	5,645	8,706	14,489
1998	6,152	2,698	11,035
1999	6,152	597	5,480
2000	6,152	1,635	963
2001	6,152	6,260	1,071
2002	5,487	6,321	1,905
2003	5,265	6,353	2,993
2004	5,265	6,402	4,130
2005	5,265	6,410	5,275
2006	5,265	6,945	6,955
2007	5,581	6,444	7,818
2008	4,748	5,203	8,273
2009	2,547	2,947	8,673
2010	2,547	2,451	8,577
2011	2,841	2,873	8,609
2012	3,253	3,529	8,885
2013	3,253	3,575	9,207
2014	3,253	3,532	9,486
2015	3,253	3,623	9,856
2016	2,440	2,863	10,279
2017	0	332	10,611
2018	1,919	2,924	11,616
2019	2,093	3,580	13,103
2020	2,093	3,256	14,266
2021	2,093	2,709	14,882
2022	2,093	3,430	16,219
2023	2,093	3,442	17,568

Under PNM's actual funding pattern, the trust assets have grown as follows:

Table 3	
($ thousands)	
Year	Trust Assets at End of Year
1993	$2,118
1994	8,559
1995	15,600
1996	20,930
1997	33,159
1998	37,602
1999	41,825
2000	44,693
2001	42,132
2002	38,925
2003	50,957
2004	56,689
2005	58,484
2006	66,790
2007	71,567
2008	49,480
2009	57,126
2010	61,749
2011	58,776
2012	64,464
2013	73,565
2014	78,175
2015	72,952
2016	72,694
2017	80,356
2018	69,703
2019	86,400
2020	93,402
2021	95,805
2022	72,843*
2023	73,527*

*Projected

If PNM had followed the exact pattern of contributions shown in Table 1, the trust assets at the end of each year would have been as follows:

Table 4 ($ thousands)	
Year	Trust Assets at End of Year
1993	$0
1994	0
1995	3,274
1996	6,307
1997	11,386
1998	16,597
1999	23,005
2000	28,926
2001	28,032
2002	26,140
2003	33,345
2004	36,099
2005	35,978
2006	39,570
2007	41,819
2008	28,070
2009	29,883
2010	29,671
2011	25,593
2012	25,569
2013	26,217
2014	25,727
2015	20,800
2016	15,680
2017	11,294
2018	6,400
2019	3,585
2020	199
2021	0
2022	0
2023	0

As can be seen in Table 2, PNM has contributed significantly more than has been required and by comparing the amounts in Tables 3 and 4, the actual assets in the PNM trusts at the end of each year were significantly greater than they would have been if PNM had followed the exact pattern of contributions in Table 1. In fact, trust assets would be depleted by the end of 2021 had PNM followed the exact pattern of contributions in Table 1. These greater assets have resulted in much lower ASC 715 expenses as seen in the following Table 5. The actual return on the trust assets in each year was used to develop the estimated numbers in Tables 4 and 5.

Using these steps, the savings on ASC 715 expense due to PNM's actual funding has been as follows:

Table 5			
($ thousands)			
Year	PNM Actual ASC 715 Expense	ASC 715 Expense Assuming Contribution Pattern in Table 1[1]	Savings
1994	$6,261	$6,446	$185
1995	8,420	9,169	749
1996	6,377	7,659	1,282
1997	5,685	6,978	1,293
1998	4,667	6,676	2,009
1999	4,866	7,361	2,495
2000	4,726	6,745	2,019
2001	9,754	11,587	1,833
2002	9,408	11,792	2,384
2003	9,682	11,804	2,122
2004	2,854	5,757	2,903
2005	4,044	6,575	2,531
2006	5,655	8,129	2,474
2007	4,541	7,404	2,863
2008	2,058	5,047	2,989
2009	1,001	3,622	2,621
2010	3,843	6,458	2,615
2011	806	3,468	2,662
2012	3,155	5,463	2,308
2013	2,229	4,931	2,702
2014	55	3,930	3,875
2015	7	4,341	4,334
2016	118	4,326	4,208
2017	910	5,516	4,606
2018	(1,202)	4,577	5,779
2019	(1,631)	3,329	4,960
2020	(2,709)	3,496	6,205
2021	(2,236)	3,478	5,714
2022	(2,427)	2,219	4,646
2023	(1,620)	2,586	4,206
2024	(1,742)	2,411	4,153
Total			95,725

[1] Once assets are depleted, it is assumed PNM would make additional contributions sufficient to satisfy benefits.

Assumptions and Methods

Except as otherwise provided herein, the results presented above are based on the data, assumptions, methods, plan provisions and other information, outlined in the actuarial valuation reports to determine accounting requirements for the plan for each fiscal year included in the analysis through 2022 and as outlined in the memo regarding the Estimated Test Year Expense Memo dated August 30, 2022 for the 2023 and 2024 fiscal years. Therefore, such information, and the reliances and limitations of the valuation reports and their use, should be considered part of this report.

BEFORE THE NEW MEXICO PUBLIC REGULATION COMMISSION

IN THE MATTER OF THE APPLICATION OF PUBLIC SERVICE COMPANY OF NEW MEXICO FOR REVISION OF ITS RETAIL ELECTRIC RATES PURSUANT TO ADVICE NOTICE NO. 595	)	**Case No. 22-00270-UT**
PUBLIC SERVICE COMPANY OF NEW MEXICO,	)	
Applicant	)	

SELF AFFIRMATION

YANNICK GAGNE, Managing Director and Actuary for Willis Towers Watson, upon penalty of perjury under the laws of the State of New Mexico, affirm and state: I have read the foregoing **Direct Testimony of Yannick Gagne** and it is true and accurate based on my own personal knowledge and belief.

Dated this 5th day of December, 2022.

/s/ Yannick Gagne
YANNICK GAGNE

GCG # 530019