

DOCKET NO. 58964

BEFORE THE PUBLIC UTILITY COMMISSION OF TEXAS

**APPLICATION OF
TEXAS-NEW MEXICO POWER COMPANY
FOR AUTHORITY TO CHANGE RATES**

**PREPARED DIRECT TESTIMONY AND EXHIBITS
OF
BRIAN ARNELL**

NOVEMBER 14, 2025

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TNMP EXHIBIT BA-1

RÉSUMÉ OF BRIAN ARNELL

TNMP EXHIBIT BA-2

**ACTUARIAL VALUATION REPORT
DISCLOSURE FOR FISCAL YEAR ENDING DECEMBER 31, 2023 AND 2024
BENEFIT COST UNDER US GAAP FOR THE TEXAS-NEW MEXICO POWER
COMPANY PENSION PLAN (HIGHLY SENSITIVE PROTECTE MATERIAL);
AND**

**ACTUARIAL VALUATION REPORT
DISCLOSURE FOR FISCAL YEAR ENDING DECEMBER 31, 2024 AND 2025
BENEFIT COST UNDER US GAAP FOR THE TEXAS-NEW MEXICO POWER
COMPANY PENSION PLAN (HIGHLY SENSITIVE PROTECTED MATERIAL)**

TNMP EXHIBIT BA-3

**ACTUARIAL VALUATION REPORT
DISCLOSURE FOR FISCAL YEAR ENDING DECEMBER 31, 2023 AND 2024
BENEFIT COST UNDER US GAAP FOR THE TEXAS-NEW MEXICO POWER
COMPANY NON-QUALIFIED RETIREMENT PLAN (HIGHLY SENSITIVE
PROTECTED MATERIAL); AND**

**ACTUARIAL VALUATION REPORT
DISCLOSURE FOR FISCAL YEAR ENDING DECEMBER 31, 2024 UNDER US
GAAP FOR THE TEXAS-NEW MEXICO POWER COMPANY NON-QUALIFIED
RETIREMENT PLAN (HIGHLY SENSITIVE PROTECTED MATERIAL)**

TNMP EXHIBIT BA-4

**ACTUARIAL VALUATION REPORT
DISCLOSURE FOR FISCAL YEAR ENDING DECEMBER 31, 2023 AND 2024
BENEFIT COST UNDER US GAAP FOR THE POST-RETIREMENT
HEALTHCARE PLAN FOR TEXAS-NEW MEXICO POWER COMPANY
RETIREEES (HIGHLY SENSITIVE PROTECTED MATERIAL); AND**

**ACTUARIAL VALUATION REPORT
DISCLOSURE FOR FISCAL YEAR ENDING DECEMBER 31, 2024 AND 2025
BENEFIT COST UNDER US GAAP FOR THE POST-RETIREMENT
HEALTHCARE PLAN FOR TEXAS-NEW MEXICO POWER COMPANY
RETIREEES (HIGHLY SENSITIVE PROTECTED MATERIAL)**

1 **I. INTRODUCTION AND PURPOSE**

2 **Q. PLEASE STATE YOUR NAME AND POSITION.**

3 A. My name is Brian Arnell. I am employed by Willis Towers Watson as a Retirement
4 Director and Pension Actuary and act as the Utility Industry Network Co-Leader for
5 WTW's Retirement business.

6 **Q. PLEASE DESCRIBE WILLIS TOWERS WATSON AND YOUR
7 QUALIFICATIONS.**

8 A. Willis Towers Watson is a leading provider of actuarial and retirement consulting
9 services. We serve as the actuary for over half of the U.S. Fortune 1000 Utilities
10 and have provided rate case support and/or testimony in most jurisdictions. We
11 have provided support and testified in several of Texas-New Mexico Power
12 Company's ("TNMP" or "Company") rate cases, including direct testimony by my
13 colleague Yannick Gagne in TNMP's most recent rate request (Docket No. 48401).
14 Personally, I have provided actuarial and consulting services for more than 18
15 years, working with regulated utilities in Texas, New Mexico and Arizona. I have
16 provided rate case support for filings in each of these states. A copy of my
17 qualifications is included in TNMP Exhibit BA – 1.

18 **Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?**

19 A. The purpose of my testimony in this proceeding is to provide background and
20 additional support related to TNMP's cost of service requests related to pension
21 benefits ("Pension") and retiree medical benefits (also referred to as Other Post-
22 Employment Benefits, or "OPEB"). Specifically, I provide supporting information
23 about the costs for the period 7/1/2024 – 6/30/2025 (the "Test Period" or "Test
24 Year") for each plan, as these costs are included in the cost of service request.
25 Additionally, I will provide information about preliminary 2025 costs, as
26 adjustments for known and measurable cost differences may be appropriate. I also
27 provide support for continued inclusion of the Prepaid Pension Asset in rate base
28 and the use of a Benefits Cost Tracker.

1 **II. EXECUTIVE SUMMARY**

2 **Q. WHAT ARE THE TEST YEAR COSTS FOR PENSION AND OPEB PLANS?**

3 A. TNMP sponsors two defined benefit pension arrangements (one qualified plan and
4 one non-qualified plan), and one retiree health care (OPEB) program.

5 Total Test Year costs (income) for all three plans are (\$708,154), attributable to
6 each plan as follows:

| Plan | Benefit Cost for Test Year |
|-----------------------|-----------------------------------|
| Qualified Pension | (\$47,237) |
| Non-Qualified Pension | \$7,741 |
| OPEB | (\$668,658) |
| Total | (\$708,154) |

7
8 These costs are made up of 6 months of the 2024 Net Periodic Benefit Cost and
9 6 months of the 2025 Net Periodic Benefit Cost for each plan.

10 **Q. SHOULD A KNOWN AND MEASURABLE ADJUSTMENT BE MADE TO THE**
11 **PENSION AND OPEB AMOUNTS?**

12 A. Yes. Because the 2025 Benefit Cost is known and will not change absent any
13 special events during the remainder of 2025, a known and measurable adjustment
14 should be made to reflect the Preliminary 2025 Benefit Costs for each plan as
15 shown in the table below:

| Plan | Preliminary 2025 Benefit Cost |
|-----------------------|--------------------------------------|
| Qualified Pension | (\$115,610) |
| Non-Qualified Pension | \$0 |
| OPEB | (\$586,162) |
| Total | (\$701,772) |

16 A.

1 **Q. HOW ARE NEGATIVE COSTS (INCOME) ADJUSTED FOR INCLUSION IN**
2 **COST OF SERVICE?**

3 When costs are less than zero, cost of service should be set to \$0 as assets cannot
4 be removed from the trust to provide reimbursement to Customers. These assets
5 remain in the trust and continue to earn a return, reducing future cost. The inclusion
6 of the Prepaid Pension Asset in rate base results in non-negative recovery for the
7 pension plan so no adjustment is required. For the OPEB plan however, a floor of
8 \$0 should be applied. The resulting amounts to be included in cost of service for
9 the pension and OPEB plans are reflected in the table below:

| Plan | Preliminary 2025 Benefit Cost |
|-----------------------|--|
| Qualified Pension | (\$115,610) |
| Non-Qualified Pension | \$0 |
| OPEB | \$0 |
| Total | (\$115,610) |

10
11 **Q. HOW DOES A PREPAID PENSION ASSET ARISE, AND WHY SHOULD A**
12 **RETURN ON THE PREPAID ASSET BE PROVIDED?**

13 A. The Prepaid Pension Asset is the result of contributions from the Company in
14 excess of the Benefit Cost under US GAAP (basis for recovery in cost of service).
15 Excess contributions increase plan assets, and reduce future costs through a
16 higher expected return on assets. In addition, a better funded plan pays lower
17 variable premium to the Pension Benefit Guaranty Corporation (“PBGC”), reducing
18 ongoing plan costs. As a result, ratepayers benefit from the Prepaid Pension Asset
19 through lower pension costs and reduced operating costs of the pension plan and
20 therefore, it is reasonable for the Company to seek a return on such Prepaid
21 Pension Asset through its inclusion in rate base.

22 In its request, the Company is limiting the amount of Prepaid Pension Asset to be
23 included in rate base so that the return it will receive is equal to the reduction in

1 Benefit Cost resulting from the existence of the Prepaid Pension Asset. In other
2 words, absent the Prepaid Pension Asset, the amount included in cost of service
3 would be higher by the amount of return provided.

4 **Q. IS THE COMPANY UTILIZING A BENEFIT COST TRACKER?**

5 A. Yes. As provided for in the Public Utility Regulatory Act (PURA) §36.065(b) and as
6 outlined in the Final Order under Docket No. 48401, the Company has adopted the
7 use of a Benefit Cost Tracker for pension and OPEB plans. This ensures that
8 recovery will be equal to actual costs, no more, no less, protecting both customers
9 and the Company. The actual benefit costs associated with these plans, with a \$0
10 floor for OPEB costs, are captured in the tracker.

11 **III. BACKGROUND**

12 **Q. WHAT PENSION AND OPEB PLANS ARE COVERED IN YOUR TESTIMONY?**

13 A. My testimony covers three plans sponsored by the Company. There are two
14 defined benefit plans and one retiree medical plan (also known as OPEB). These
15 are:

- 16 • The Texas-New Mexico Power Company Pension Plan (“Qualified Pension
17 Plan”), a qualified defined benefit plan as defined by the Employee
18 Retirement Income Security Act (“ERISA”);
- 19 • The Texas-New Mexico Power Company Non-Qualified Retirement Plan
20 (“Non-qualified Retirement Plan”) a non-qualified defined benefit plan as
21 defined by ERISA; and
- 22 • The Post-Retirement Healthcare Plan for the Texas-New Mexico Power
23 Company Retirees (“OPEB” or “Retiree Medical”), which provides for
24 medical and nominal life insurance coverage for certain retirees.

25 **Q. WHAT AMOUNTS DOES THE COMPANY SEEK TO RECOVER IN THIS
26 PROCEEDING FOR ITS PENSION AND OPEB PLANS?**

27 A. The amounts that TNMP proposes to recover in rates here are comprised of three
28 components:

- 1 1) An amount equal to the annual Benefit Cost (“expense”) (not less than \$0
2 for the OPEB plan) calculated under applicable accounting standards
3 (Accounting Standards Codification (“ASC”) 715-30 for pensions and ASC
4 715-60 for OPEB); plus
- 5 2) For Pensions, a return on amounts contributed by shareholders to the
6 pension plan in excess of cumulative annual pension expenses via inclusion
7 of the Prepaid Pension Asset in rate base; plus
- 8 3) Amortization of amounts captured in the Benefit Cost Tracker

9 **Q. HAS THE COMPANY BEEN ALLOWED TO RECOVER THESE CATEGORIES**
10 **OF COSTS IN PRIOR PROCEEDINGS?**

11 A. The Company’s current rates were established under a settlement that was
12 approved in Docket No. 48401. It is my understanding that the settlement
13 effectively allowed for recovery of amounts analogous to the first two items outlined
14 above, although I understand that settled cases do not have the force of precedent.
15 Further, the final Order in the same Docket allowed for the Company to establish
16 a Benefit Cost Tracker resulting in the third item above.

17 **Q. WHY DO COSTS FOR THOSE BENEFIT PROGRAMS CONTINUE EVEN**
18 **AFTER THE PLANS WERE CLOSED OR FROZEN?**

19 A. While pension and OPEB benefits will accrue over an employee’s career, the
20 employer obligations generally continue for the employee’s lifetime and sometimes
21 the lifetime of their spouse or beneficiary. The actual costs of providing those
22 benefits will not be exactly known until all promised benefits have been paid as
23 participants may live longer than expected, plan assets may earn more or less than
24 expected, or interest rates may change. This means costs associated with those
25 plans will continue well after new pension benefits have ceased to accrue or
26 employees have left the Company. Therefore, ongoing costs associated with
27 fulfilling the Company’s obligations continue to be a necessary and reasonable
28 cost and should be included in cost of service.

1 **Q. PLEASE DESCRIBE THE ACCOUNTING TREATMENT FOR TNMP'S PENSION**
2 **PLANS.**

3 TNMP accounts for its pension plans in accordance with ASC 715-30. ASC 715-
4 30 requires that the unfunded projected benefit obligation (i.e. the difference
5 between the value of the pension plan assets and the projected benefit obligation)
6 be recognized as a liability on the balance sheet. Prior service costs and unrealized
7 actuarial gains or losses are recorded to a Regulatory Asset/Liability and are
8 systematically recognized as an expense over subsequent periods, which TNMP
9 recovers through pension expense.

10 FERC Docket No. AI07-1-000 provides further guidance regarding accounting for
11 defined benefit postretirement plans which allows entities to recognize regulatory
12 assets for amounts otherwise chargeable to Accumulated Other Comprehensive
13 Income under ASC 715-30 to the extent that they are recoverable in rates in future
14 periods.

15 **Q. HOW ARE BENEFIT COSTS CALCULATED?**

16 A. Under ASC 715, Benefit Costs are made up of several components including:

17 (1) the value of benefits that employees will earn during the current year (Service
18 Cost)

19 (2) increases in the present value of the benefits that plan participants have earned
20 in previous years due to interest (Interest Cost),

21 (3) a reduction for investment earnings on plan assets that are expected to be
22 earned during the year (Expected Return on Assets),

23 (4) recognition of the cost of benefit changes the plan sponsor provides for service
24 the employees have already performed (amortization of Unrecognized Prior
25 Service Cost), and

26 (5) recognition of costs (or income) from experience that differs from the
27 assumptions (e.g., investment earnings different than assumed) (amortization of
28 Unrecognized Gains and Losses, Settlement and/or Curtailment recognition of
29 Gains and Losses, etc.).

1 **Q. PLEASE DESCRIBE EACH OF THE COMPONENTS OF BENEFIT COST**

2 A. These components are described below:

3 1) Service Cost

4 The service cost component of NPBC is the “actuarial present value” of the
5 benefits attributed by the benefit formula for the year and expected to be earned
6 during the year reflecting projected pay to expected retirement age. An attribution
7 method is adopted to reflect a reasonable pattern of benefit accrual for recognition
8 purposes. For the test year, the actuary used certain assumptions to estimate the
9 Company-provided share of the benefits to be earned by an employee during the
10 year and determined the present value of these benefits (i.e., the service cost).

11 2) Interest Cost

12 Interest cost is the increase in the present value of the projected benefit obligation
13 (“PBO”) for pension plans or the accumulated postretirement benefit obligation
14 (“APBO”) for other postretirement benefit plans due to the passage of one year’s
15 time. The PBO is an estimate of present value of pension benefits accrued through
16 the valuation date using projected salary levels and based on assumptions,
17 including the discount rate, outlined in the actuarial valuation. The APBO is the
18 present value of other postretirement benefits (e.g., postretirement medical and
19 life benefits) based on the substantive plan and attribution method based on
20 assumptions including a discount rate, outlined in the actuarial valuation. The
21 present values of the PBO and APBO are discounted amounts based on an
22 assumed discount rate.

23 3) Expected Return on Assets

24 The expected return on plan assets is also used in the computation of Net Periodic
25 Benefit Cost for the year. The Company’s overall costs are reduced by earnings
26 on assets that have been accumulated with contributions to the benefit funds. An
27 expected return assumption is selected by the Company based on the asset
28 allocation of the trust and long-term return expectations of the various asset
29 classes held by the trust. The actual return on plan assets includes the plan’s

1 dividend and interest income for the year, plus realized and unrealized
2 appreciation less any depreciation in the market value of its investments and the
3 expenses related to benefits paid, administration and investing the fund. The
4 difference between the expected return on assets and the actual return on assets
5 is recognized through gains and losses.

6 4) Amortization of Transition Obligation

7 The amortization of transition obligation is the difference between the fair market
8 value of plan assets and the actuarial present value of benefits earned at the time
9 of transition to the provisions of SFAS 87 and SFAS 106. TNMP's transition
10 obligation has been fully amortized.

11 5) Recognition of Prior Service Cost

12 The recognition of prior service cost is the amortization of a change in the projected
13 benefit obligation due to a plan amendment. Under ASC 715 increases or
14 decreases in the PBO or APBO due to a plan change are amortized as a
15 component of future costs over the average remaining service lives of active
16 employees expected to receive benefits at the time of the amendment.

17 6) Recognition of Gains and Losses

18 Gains and losses are changes in the amount of either the obligation or the plan
19 assets different from expectations. These changes result from experience that is
20 different from what is expected (such as asset returns being more or less than the
21 expected return assumption, salary increases being more or less than anticipated,
22 employees retiring at different ages than expected, retirees living shorter or longer
23 than expected, etc.) and from changes in assumptions (different discount rates
24 from year to year or changes in demographic assumptions based on plan
25 experience).

26 If accumulated gains and losses are greater than a "corridor" amount, a portion
27 outside the corridor is recognized in the current year (determined as the excess
28 over the corridor amortized over the average remaining life expectancy for pension
29 benefits, and average remaining service lives of active employees expected to

1 receive benefits under the plan for OPEB). The corridor is 10% of the greater of
2 the PBO (or APBO) and the market-related value of assets.

3 In certain circumstances, ASC 715-30 requires modifications to the recognition of
4 gains or losses to better align the timing of recognition with the actual lifecycle of
5 the plan. This may occur, for example, if a material number of plan participants
6 elect to receive their benefits as a lump sum.

7 **Q. WHAT IS THE BASIS FOR DETERMINING THE AMOUNT OF BENEFIT COSTS**
8 **TO BE INCLUDED IN THE REVENUE REQUIREMENTS RELATED TO THE**
9 **PENSION AND OPEB PLANS IN THIS RATE CASE?**

10 A. The amount included in revenue requirements for pensions and OPEB are equal
11 to the actual pension and retiree medical Net Periodic Benefit Costs for the Test
12 Year. Willis Towers Watson has prepared those calculations and the results are
13 presented below. Please see TNMP Exhibits BA-2, BA-3, and BA-4 for detailed
14 calculations for the Test Year cost for each plan.

15 **Q. WHAT ARE THE KEY ASSUMPTIONS USED IN CALCULATING THOSE**
16 **COSTS?**

17 A. Because these plans involve benefits to be paid far into the future, several
18 assumptions must be made about things such as when will participants leave
19 employment, commence benefits, as well as how long participants will live. Once
20 the plan actuary has projected all future benefit payments expected to be made
21 (when and how much), those payments are discounted to today using an assumed
22 discount rate. Another key component of the cost is the expected return on plan
23 assets. Both the discount rate and the expected return on asset are key economic
24 assumptions.

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

27 A. The discount rate is the rate used to discount projected benefit payments under
28 the plan to today. Discount rates are the same as those used by the Company for
29 its corporate financial statements following the same methodology for many years.

1 The discount rate is reviewed for reasonableness by a number of independent
2 parties such as corporate auditors and the plan actuary.

3 The discount rate assumption for each plan is selected by creating a hypothetical
4 portfolio of high-quality bonds in which cash flows (coupons and maturities) match
5 the projected benefit payments from the plan. The effective interest rate of the
6 resulting portfolio (interest rate at which discounted coupons and maturities equal
7 the market price of the underlying bonds) is the discount rate. While several
8 different methodologies may be acceptable (such as applying the plan's projected
9 benefit payments to a yield curve), accounting standards require that the discount
10 rate methodology be applied consistently year after year, unless the plan's
11 circumstances have materially changed so that the methodology no longer
12 provides management's best estimate. For the 2024 costs, discount rates were
13 5.47% for pensions and 5.48% for OPEB and for the 2025 costs, the discount rates
14 was 5.78% for both pensions and OPEB. I believe the discount rate assumptions
15 are reasonable.

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

18 A. The expected return on asset assumption is used in the Benefit Cost calculation.
19 The Benefit Cost is reduced by the investment returns expected to be generated
20 by the plan assets, calculated based on this assumption. The expected return on
21 asset assumption is based on the same methodology used for the Company's
22 corporate financial statements and is subject to the same external review as
23 discount rates. It is made up of two components:

- 24 a) An expected return resulting from plan assets invested passively in the
25 various asset classes (similar to index funds, for example a fund that
26 matches returns of the S&P 500), reflecting the plan's target asset
27 allocation, plus
- 28 b) An additional return resulting from active management of the assets (also
29 known as manager alpha). This amount is determined based on historical
30 performance for the various TNMP plans.

1 The final result is also adjusted to reflect the effect of taxation on any returns. For
 2 the 2024 costs, expected return on asset assumptions are 5.95% for pensions,
 3 and 5.25% for OPEB and for the 2025 costs, expected return on asset
 4 assumptions are 7.00% for pensions and 5.55% for OPEB. I believe those
 5 assumptions are reasonable.

6 **IV. TEST YEAR COSTS**

7 **Q. WHAT ARE THE NET PERIODIC BENEFIT COSTS FOR THE QUALIFIED**
 8 **PENSION PLAN, NON-QUALIFIED PENSION PLAN, AND OPEB PLAN FOR**
 9 **THE TEST YEAR?**

10 A. The total Net Periodic Benefit Cost for all three plans for the Test Year is
 11 (\$708,154). These costs are made up of 6 months of the 2024 Net Periodic Benefit
 12 Cost and 6 months of the 2025 Net Periodic Benefit Cost for each plan. The Net
 13 Periodic Benefit Cost is the Benefit Cost in the fiscal year excluding gain and loss
 14 recognitions caused by a change in the expected lifetime of the plan which are not
 15 anticipated to recur in the future. TNMP Exhibits BA-2, BA-3, and BA-4 provide
 16 details as to how the 2024 and 2025 amounts are calculated for each plan. The
 17 table below summarize the cost by plan:

| Plan | Net Periodic Benefit Cost for 2024 | Net Periodic Benefit Cost for 2025 | Benefit Cost for Test Year |
|-----------------------|---|---|---------------------------------------|
| Qualified Pension | \$21,137 | (\$115,610) | (\$47,237) |
| Non-Qualified Pension | \$15,482 | \$0 | \$7,741 |
| OPEB | (\$751,153) | (\$586,162) | (\$668,658) |
| Total | (\$714,534) | (\$701,772) | (\$708,154) |

18
 19 **Q. ARE THESE COSTS NECESSARY AND REASONABLE COSTS FOR**
 20 **PROVIDING PENSION AND OPEB BENEFITS TO EMPLOYEES?**

21 A. Yes. In defined benefit and OPEB plans, the Company promises to provide
 22 benefits for the employees' lifetime. Therefore, the actual cost for providing those

1 benefits will not be known until all promised payments have been made. The
 2 Benefit Cost provides an objective and systematic way to recognize those costs
 3 over time. These costs are therefore necessary to fulfill the benefit promises made
 4 to employees and former employees.

5 **Q. WHAT ARE THE PRELIMINARY 2025 BENEFIT COSTS FOR THE PLANS?**

6 A. Preliminary 2025 Benefit Costs for each plan are reflected in the table below:

| Plan | Preliminary 2025 Benefit Cost |
|-----------------------|--|
| Qualified Pension | (\$115,610) |
| Non-Qualified Pension | \$0 |
| OPEB | (\$586,162) |
| Total | (\$701,772) |

7

8 **Q. ARE YOU RECOMMENDING A KNOWN AND MEASURABLE ADJUSTMENT**
 9 **TO REFLECT THE PRELIMINARY 2025 BENEFIT COSTS?**

10 A. Yes. The 2025 costs are the most up to date measure of the costs associated with
 11 the pension and OPEB benefits and better reflect the ongoing costs of the plans
 12 compared to the Test Year costs.

13 **Q. WHAT ARE THE MAIN REASONS FOR THE CHANGE IN COSTS BETWEEN**
 14 **THE TEST YEAR AND 2025?**

15 A. The decrease in cost for the Qualified Pension is driven primarily by an increase
 16 in the Expected Return on Asset assumption. Due to anticipated changes in the
 17 asset mix, the expected return on asset assumption increased from 5.95% in 2024
 18 to 7.00% for 2025. For OPEB, the increase in cost is due primarily to assets
 19 returning less than assumed. For the Non-Qualified Pension, the cost is zero
 20 because the final surviving plan participant passed away during 2024. No further
 21 benefits are owed to any individual and all costs associated with the plan have
 22 been recognized.

23 **Q. WHY ARE 2025 AMOUNTS LABELED PRELIMINARY, WILL THEY CHANGE?**

1 A. The 2025 net periodic costs shown above are expected to be final, unless a special
2 event occurs during the year that would require the plan to be re-measured. We
3 are not aware of any such events occurring or being likely to occur in 2025.

4 **Q. WHAT CAUSES THE BENEFIT COST TO BE NEGATIVE (AN INCOME)?**

5 A. As stated previously, under ASC 715, benefit costs consist of several components,
6 one of which is a reduction for expected investment earnings on plan assets during
7 the year (Expected Return on Assets). The net benefit cost is negative (an income)
8 because the Expected Return on Assets (combined with gains being amortized in
9 the OPEB plan) is greater than the sum of all other components of the benefit cost.

10 **Q. CAN PENSION OR OPEB ASSETS, OR RETURNS ON THOSE ASSETS, BE**
11 **ACCESSED BY THE COMPANY FOR ANY PURPOSE OTHER THAN TO PAY**
12 **FOR BENEFITS?**

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

16 **Q. WHAT ADJUSTMENT SHOULD BE MADE TO THE OPEB AMOUNT**
17 **INCLUDED IN COST OF SERVICE?**

18 A. Because the plan assets must remain in the trust, the amount included for the
19 OPEB plan in cost of service should be set at \$0. Reducing cost of service to reflect
20 the negative cost would require TNMP to pull the assets from the trusts to offset
21 other costs, which TNMP cannot legally do. Because the assets remain in the
22 trusts and cannot be used for other purposes, customers retain the benefit.
23 Applying a negative adjustment to cost of service would result in a "double benefit"
24 to customers as they would benefit from a rate reduction and benefit again from
25 the same amount being available to pay for future benefits.

26 **Q. WHY IS IT APPROPRIATE FOR THE PENSION AMOUNT INCLUDED IN COST**
27 **OF SERVICE TO BE LESS THAN \$0?**

28 A. As discussed further in my testimony, TNMP proposes to include a portion of the
29 Prepaid Pension Amount in rate base. The portion of the Prepaid Pension Asset
30 included in rate base is such that the resulting return is equal to the reduction in

1 pension benefit cost attributable to the Prepaid Pension Asset. When combined
 2 with the benefit cost, this results in non-negative recovery making a \$0 floor
 3 unnecessary.

4 **Q. WHAT ARE THE FINAL AMOUNTS TO BE INCLUDED IN COST OF SERVICE**
 5 **FOR THE PENSION AND OPEB PLANS?**

6 A. After reflecting the known and measurable adjustment described above and
 7 limiting OPEB costs to not less than \$0, the amounts included are as follows:

| Plan | Benefit Cost for Test Year | Known and Measurable Adjustment | Included in Cost of Service |
|-----------------------|----------------------------|---------------------------------|-----------------------------|
| Qualified Pension | (\$47,237) | (\$115,610) | (\$115,610) |
| Non-Qualified Pension | \$7,741 | \$0 | \$0 |
| OPEB | (\$668,658) | (\$586,162) | \$0 |
| Total | (\$708,154) | (\$701,772) | (\$115,610) |

8

9 **V. PREPAID PENSION ASSET**

10 **Q. IS TNMP ALSO SEEKING TO INCLUDE IN RATE BASE AN AMOUNT**
 11 **RELATED TO ITS PREPAID PENSION ASSET?**

12 A. Yes. As addressed by TNMP Witness Kyle Sanders, TNMP seeks to include an
 13 amount in rate base to reflect the Prepaid Pension Asset. The Prepaid Pension
 14 Asset represents the accumulated amounts contributed to the pension plan in
 15 excess of the Benefit Cost for the plan.

16 It is important to note that for the qualified plan, the full amount of prepaid asset
 17 (approximately \$19.7 million at June 30, 2025) is available to satisfy plan
 18 obligations. Therefore, TNMP could ask to include the full Prepaid Pension Asset
 19 in rate base. However, TNMP limits the amount to be included in rate base to \$18.9
 20 million to ensure that the return it will receive from the inclusion in rate base only
 21 offsets the reduction in Benefit Cost resulting from those additional contributions.

1 **Q. HOW ARE CASH CONTRIBUTIONS TO THE QUALIFIED PENSION PLAN**
2 **DETERMINED?**

3 A. The funding of a pension plan is determined based upon prudent business
4 practices within the following legal constraints of the Employee Retirement Income
5 Security Act (“ERISA”), as modified by the Pension Protection Act (“PPA”), and the
6 Internal Revenue Code (“IRC”):

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

11 The minimum and maximum funding rules set forth under ERISA, the PPA, and
12 the IRC use accrual methodologies, but they are different from the methodology
13 used under ASC715-30. Over the long run, the cumulative employer cash
14 contributions made to a plan and the cumulative annual pension cost amounts
15 should be equal. But in the short and intermediate run, there can be significant
16 differences.

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

23 **Q. WERE ANY COMPANY CASH CONTRIBUTIONS MADE IN 2024 OR 2025 TO**
24 **DATE OR FORECASTED FOR THE REMAINDER OF 2025 TO THE QUALIFIED**
25 **PENSION PLAN?**

26 A. In 2024 the company contributed \$151,230 to the pension plan. No contributions
27 have been made or are forecasted for the remainder of 2025. While at December
28 31, 2024 (last formal measurement date for TNMP’s financial statements), the
29 pension plan shows an unfunded Projected Benefit Obligation (“PBO”) of just

1 under \$1 million, no contributions have been or are planned to be made in 2025.
2 This is the result of a number of changes to minimum funding rules enacted by
3 Congress over the past decade, which resulted in a reduction in minimum required
4 contributions for qualified pension plans. As a result, the current funding balances
5 are projected to be sufficient to satisfy all minimum funding requirements in the
6 near term.

7 **Q. PLEASE EXPLAIN HOW ADDITIONAL CONTRIBUTIONS AFFECT BENEFIT**
8 **COST.**

9 A. As mentioned previously, one of the components of pension expense is the
10 Expected Return on Asset (“EROA”). The pension expense is reduced by the
11 investment returns expected to be earned on the plan assets. Therefore, each
12 dollar of additional contribution will reduce the Benefit Cost – and consequently the
13 amount charged to ratepayers – by an amount equal to the expected return on
14 such additional contributions. At June 30, 2025, plan assets include a Prepaid
15 Asset (or additional contributions) of \$19.7 million. If the additional contributions
16 that created this Prepaid Asset had not been made, the pension expense for the
17 following year would be \$1.4 million higher using the 7.00% expected return on
18 assets assumption for 2025 (\$19.7 million x 7.00%).

19 **Q. ARE THERE BENEFITS TO ACCELERATED FUNDING?**

20 A. Yes. Once amounts are contributed to the pension trusts, they are invested and
21 earn returns. Each dollar of return reduces future contributions that will be needed
22 to satisfy plan obligations. In addition to the returns generated on invested assets,
23 additional funding reduces the amount of variable premium the plan must pay to
24 the Pension Benefit Guaranty Corporation (“PBGC”). The TNMP pension plan was
25 subject to variable premiums in both 2023 and 2024.

26 **Q. WHAT IS THE PBGC?**

27 A. The PBGC is a federal agency established by Congress as part of ERISA to protect
28 pension benefits under private sector defined benefit pension plans. If a pension
29 plan is terminated without sufficient funds to pay all benefits, the PBGC will pay
30 employees the benefits promised under the plan, up to certain limits set by law.

1 Funding for the PBGC comes from premiums charged to pension plans as well as
2 returns on assets held by the PBGC.

3 **Q. WHAT TYPES OF PREMIUMS DOES THE PBGC CHARGE?**

4 A. The PBGC charges two types of premiums: (1) a per capita premium charged to
5 all single employer defined benefit plans, and (2) a variable premium charged to
6 underfunded plans, on a measure defined by the PBGC.

7 **Q. HOW MUCH IS THE PBGC VARIABLE PREMIUM?**

8 A. Through 2013, the PBGC variable premium was 0.9% of any unfunded liability.
9 For this purpose, the liability is measured based on assumptions set by the PBGC.
10 This liability measure is often different from the PBO used for pension cost
11 purposes under ASC 715 and is much higher than the funding liability used for
12 minimum required contribution purposes.

13 **Q. WHAT HAPPENED TO THE AMOUNT OF VARIABLE PREMIUM RATES
14 AFTER 2013?**

15 A. Effective in 2014, Congress passed a law increasing the variable premium rate.
16 The new law increased the 0.9% of unfunded liability premium to 1.4% in 2014,
17 and 2.4% for 2015. As part of the 2015 Budget Act, Congress further increased
18 variable premium rates to 3.0% for 2016 increasing annually thereafter until 2024
19 when indexation was stopped as part of the SECURE 2.0 Act. For 2025 and
20 beyond, the variable rate premium is 5.2% of unfunded liabilities (subject to per
21 participant maximums). These variable premium increases significantly add to the
22 benefit of accelerated contributions.

23 **Q. WHAT IS THE IMPACT OF THE PREPAID PENSION ASSET ON THE PBGC
24 VARIABLE PREMIUM FOR THE TNMP PENSION PLAN?**

25 A. The plan has been underfunded on a PBGC basis, and the prepaid asset reduced
26 the PBGC deficit dollar for dollar. This means that the prepaid pension asset
27 effectively generates an additional 5.2% return (via cost reduction) above any
28 investment returns.

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

4 A. Yes. As noted previously, the Company's current rates were established under a
5 settlement that was approved in Docket No. 48401. The Prepaid Pension Asset
6 was included in rate base in the Company's proposal and this was not adjusted in
7 the settlement agreement and was therefore included in the final approved rates.
8 I understand that settled cases do not have the force of precedent.

9 In its 2013 decision in a SWEPCO rate proceeding in Docket No. 40443, the
10 Commission approved rate base treatment for a similar Prepaid Pension Asset.
11 Referencing Statement of Financial Accounting Standards No. 87, the
12 Commission found that "the prepaid pension asset represents the amount by which
13 the accumulated contributions exceed the accumulated FAS 87 pension fund
14 cost." That definition applies equally to the prepaid pension asset TNMP proposes
15 to include in rate base here. The Commission concluded that the "portion of
16 SWEPCO's prepaid pension asset associated with pension cost charged to O&M
17 expense is appropriately included in rate base" and approved a corresponding
18 ADIT rate base adjustment. I believe the Prepaid Pension Asset treatment
19 proposed by TNMP in this request is appropriate and consistent with the precedent
20 from SWEPCO.¹

21 **Q. IF RECOVERY OF THE COSTS OF THE PREPAID PENSION ASSET WERE**
22 **DISALLOWED, WHAT OFFSETTING ADJUSTMENTS WOULD HAVE TO BE**
23 **MADE TO TNMP'S COST OF SERVICE?**

24 A. Any amount disallowed from rate base signifies that the Commission considers
25 that amount to belong to shareholders. As a result, the Benefit Cost included in the
26 cost of service must be increased by the expected return on the amount being
27 disallowed. In addition, the Accumulated Deferred Income Taxes balance

¹ *Application of Southwestern Electric Power Company For Authority to Change Rates and Reconcile Fuel Expenses, Docket No. 40443, Order at Finding of Fact No. 130, 134 (Oct. 10, 2013).*

1 associated with the prepaid pension asset (rate base reduction) must also be
2 adjusted.

3 **VI. BENEFIT COST TRACKER**

4 **Q. WHY DO PENSION (AND OPEB) COSTS VARY YEAR OVER YEAR?**

5 A. Under a pension plan, the amount of benefit earned by the employees is set by
6 formula. The employer will set aside funds to pay for those benefits once
7 employees retire. Because the ultimate benefit is not known until the employee
8 retires, annual costs will vary (sometimes significantly) based on factors such as
9 asset returns, interest rates, and other demographic experience. Most of those
10 factors (for example interest rates, investment markets, mortality, etc.) are outside
11 of the control of the Company. The same principles apply to OPEB plans.

12 **Q. WHAT RISKS DOES THAT ANNUAL VOLATILITY CAUSE TO THE COMPANY
13 AND THE RATEPAYERS?**

14 A. A major risk of basing recovery on Test Year cost, is that actual future costs may
15 differ significantly. If future costs are lower, the Company profits from the windfall.
16 If costs are higher, the Company does not receive appropriate reimbursements.

17 **Q. HAS THERE BEEN VOLATILITY IN BENEFIT COST SINCE THE PRIOR RATE
18 REQUEST?**

19 A. Yes. Benefit costs for each plan have varied in recent years based on movements
20 in interest rates and asset performance. Additionally, as required by ASC 715-30,
21 a portion of the qualified pension plans unrecognized gains and losses were
22 recognized in years where participant elections of the lump sum form of payment
23 exceeded the relevant threshold and in the non-qualified plan all remaining
24 unrecognized gains and losses were recognized when the last participant passed
25 away.

26 **Q. HAS THE COMPANY ADOPTED A BENEFIT COST TRACKER TO CAPTURE
27 THE ACTUAL COSTS IN THESE YEARS AND IN THE FUTURE?**

28 A. Yes. As provided for in the Public Utility Regulatory Act (PURA) §36.065(b) and as
29 outlined in the Final Order under Docket No. 48401, the Company has adopted the
30 use of a Benefit Cost Tracker for pension and OPEB plans. This ensures that

1 recovery will be equal to actual costs, no more, no less, protecting both customers
2 and the Company. Please refer to the testimony of TNMP Witness Kyle Sanders
3 for details regarding the treatment of the Benefits Tracker reserve accounts.

4 **Q. HOW SHOULD THE FLOOR OF \$0 ON THE OPEB COST BE APPLIED TO THE**
5 **BENEFIT COST TRACKER?**

6 A. The floor of \$0 will also be applied to the actual benefit cost captured in the tracker.
7 To the extent actual benefit cost for a year is less than \$0, the cost used for tracker
8 calculations will also be set to \$0 as this will ultimately be the actual amount
9 recovered for these benefits over time and, as described earlier, allowing recovery
10 to be less than \$0 would result in a double benefit for customers.

11 **VII. CONCLUSION**

12 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

13 A. Yes.

AFFIDAVIT

STATE OF Arizona §
 §
COUNTY OF Maricopa §

BEFORE ME, the undersigned authority, on this day personally appeared Brian Arnell, who, upon proving his identity to me and by me being duly sworn, deposes and states the following:

“My name is Brian Arnell. I am of legal age, a resident of the State of Arizona, and have never been convicted of a felony. I certify that the foregoing testimony, offered by me on behalf of Texas-New Mexico Power Company, is true and correct and based upon my personal knowledge and experience.”

Brian Arnell
Witness

* * * * *

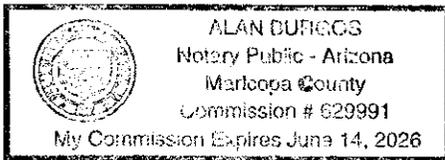
SWORN TO AND SUBSCRIBED before me, Notary Public, on this 3rd day of Nov, 2025, to certify which witness my hand and seal of office.

Alan Burgos
NOTARY PUBLIC in and for the
State of - Arizona

Printed Name: Alan Burgos

My Commission expires: 6.14.26

Notary ID# 629991



**Statement of Qualifications for
Brian Arnell**

Current Responsibilities and Experience:

I have over 15 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 Retirement Director and Actuary.

Education:

Bachelor of Science – Actuarial Science
Brigham Young University

Employment:

Willis Towers Watson (formerly Towers Watson & Company)
Director, Retirement and Actuary
Retirement Business Utility Industry Network Co-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 15 years of retirement consulting experience, I have helped company leaders understand the financial and people implications of their retirement programs and assisted them in making decisions to design and manage these plans in a way that best meet the needs of their company.

In particular, I have provided services to a number of regulated utilities including testimony support in rate case proceedings, as well as retirement program design and financial management support. Specifically regarding rate cases, I have supported both electric and gas rate case filings in New Mexico, Arizona, and Texas.

This information contains highly sensitive protected material and will be made available only after execution of a certification to be bound by the draft protective order set forth in Section VII of this Rate Filing Package or a protective order issued in this docket.

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APPLICATION OF TEXAS-NEW MEXICO POWER COMPANY
FOR AUTHORITY TO CHANGE RATES

WORKPAPERS FOR
THE DIRECT TESTIMONY OF
BRIAN ARNELL

TNMP Witness Brian Arnell has no supporting workpapers for his direct testimony.