

4. Regarding the volatility of financial statement results, discussed in paragraph 18 of the Petition, reflecting the annual swings of equity market returns without smoothing generates significant volatility of total net periodic pension expense. Of primary concern to users of the financial statements is the service cost, which is the component of pension expense that is included in operating costs as a compensation expense and represents the benefits earned by employees during the year. This measure is not impacted by asset performance. Also of primary concern are the cash contributions the sponsor will need to make to the plan.
5. By point of reference, the determination of the required cash contributions to pension plans by companies that maintain large plans generally employs significant smoothing methodologies, with asset returns smoothed over a 24-month period and interest rates averaged over 25 years.
6. Regarding the impact asset smoothing will have on pension cost volatility, as discussed in paragraph 25 of the Petition, the amortization of net gain or loss has been a significant source of volatility, with a standard deviation of \$36M over the period 2009 - 2022. As demonstrated by the simplified example below, the use of asset smoothing, and the corresponding impact on the gain or loss amortization, significantly reduces volatility of pension costs associated with market returns.
7. PSEG had approximately \$6.9B in pension assets as of the end of 2021. If pension assets return -10% during 2022, plan assets would decline by approximately \$690M. Assuming an expected return of approximately \$500M, this scenario would create an experience loss of \$1,190M. The following table outlines the impact on pension expense of an investment loss of this magnitude under the current and proposed asset valuation method. Note certain simplifications have been made for purposes of this exhibit. The actual calculations reflect certain other parameters and therefore would be slightly different.

**Current Method—Fair Value of Assets (amounts in \$millions)**

Year	2022 Experience Loss Reflected <sup>1</sup>	Loss Reflected but Not Yet Amortized <sup>2</sup>	Impact on Loss Amortization <sup>3</sup>
2023	\$1,190	\$1,190	\$74 (\$1,190 ÷ ~16)
2024	\$0	\$1,116 (\$1,190 - \$74 + \$0)	\$70 (\$1,116 ÷ ~16)
2025	\$0	\$1,046 (\$1,116 - \$70 + \$0)	\$65 (\$1,046 ÷ ~16)
2026	\$0	\$981 (\$1,046 - \$65 + \$0)	\$61 (\$981 ÷ ~16)
2027	\$0	\$920 (\$981 - \$61 + \$0)	\$58 (\$920 ÷ ~16)

**Proposed Method—Calculated Market-Related Value of Assets (amounts in \$millions)**

Year	2022 Experience Loss Reflected <sup>4</sup>	Loss Reflected but Not Yet Amortized <sup>5</sup>	Impact on Loss Amortization <sup>6</sup>
2023	\$238 (20% x \$1,190)	\$238	\$15 (\$238 ÷ ~16)
2024	\$238 (20% x \$1,190)	\$461 (\$238 - \$15+ \$238)	\$29 (\$461 ÷ ~16)
2025	\$238 (20% x \$1,190)	\$670 (\$461 - \$29+ \$238)	\$42 (\$670 ÷ ~16)
2026	\$238 (20% x \$1,190)	\$866 (\$670 - \$42+ \$238)	\$54 (\$866 ÷ ~16)
2027	\$238 (20% x \$1,190)	\$1,050 (\$866 - \$54 + \$238)	\$66 (\$1,050 ÷ ~16)

<sup>1</sup> Under the current method the entire loss of \$1,190 is reflected immediately for purposes of calculating pension expense.

<sup>2</sup> Represents prior year loss not yet amortized, minus prior year amortization, plus portion of loss reflected in the current year.

<sup>3</sup> Losses are generally amortized over a 16-year period. Actual loss amortization periods vary by Plan.

<sup>4</sup> Under the proposed methodology only 20% of the loss incurred in 2022 is reflected each year for purposes of calculating pension expense.

<sup>5</sup> As in the prior table, represents prior year loss not yet amortized, minus prior year amortization, plus portion of loss reflected in the current year.

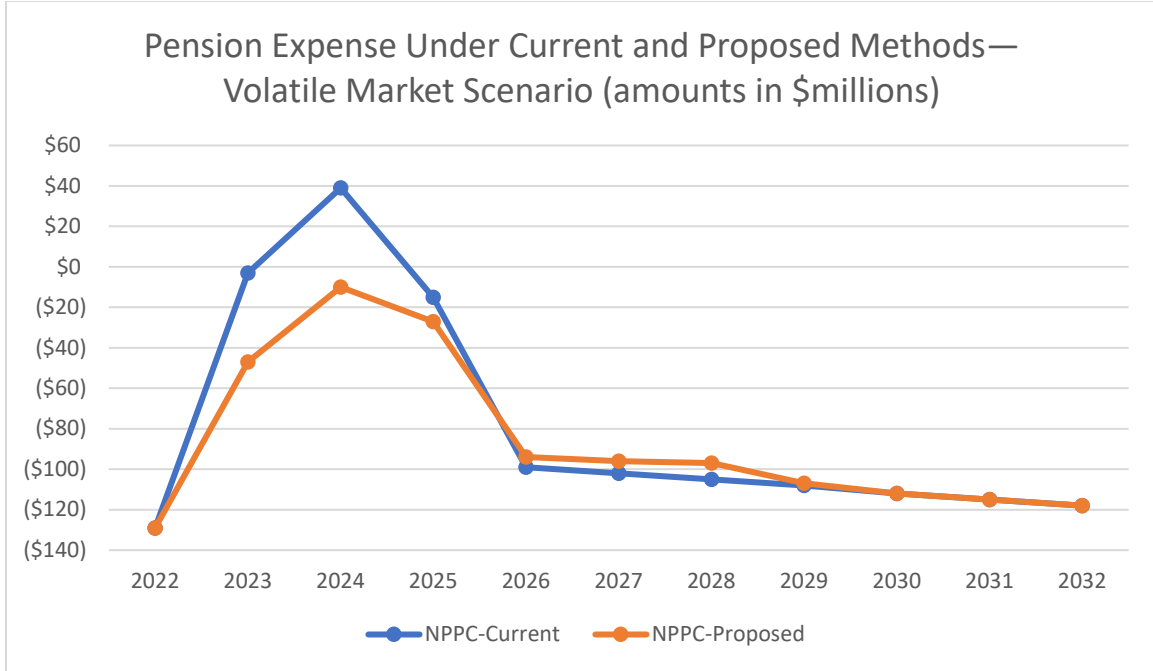
<sup>6</sup> As in the prior table, losses are generally amortized over a 16-year period. Actual loss amortization periods vary by Plan.

8. The tables above illustrate the volatility dampening effect of asset smoothing of a single year investment loss. Under the current method, the impact on the loss amortization is significant in the first year while under the proposed method the impact gradually builds over time.
9. In order to further demonstrate the volatility reduction achieved under the proposed methodology on the Net Periodic Pension Cost (“NPPC”), the following scenario assumes volatile market returns over the period 2022 – 2025, followed by consensus market returns thereafter. Based on this volatile profile of market returns, we determine pension expense under the current and proposed methodology to illustrate how the use of smoothing in the calculation of the market-related value of assets, and the corresponding impact on the gain or loss amortization, can significantly dampen pension cost volatility.

**Pension Expense Under Current and Proposed Methods—Volatile Market Scenario  
(amounts in \$millions)**

Year	Pension Trust Asset Return <sup>7</sup>	Pension Expense/(Income) Allocable to PSE&G—Current Methodology	YOY Change – current method	Pension Expense Allocable to PSE&G—Proposed Methodology	YOY change – proposed method
2022	-17.0%	\$(129)		\$(129)	
2023	0.0%	\$(3)	126	\$(47)	82
2024	+20.0%	\$39	42	\$(10)	37
2025	+30.0%	\$(15)	54	\$(27)	17
2026	+6.8%	\$(99)	84	\$(94)	67
2027	+6.8%	\$(102)	3	\$(96)	2
2028	+6.8%	\$(105)	3	\$(97)	1
2029	+6.8%	\$(108)	3	\$(107)	10
2030	+6.8%	\$(112)	3	\$(112)	5
2031	+6.8%	\$(115)	3	\$(115)	3
2032	+6.8%	\$(118)	3	\$(118)	3
Average YOY change in pension expense during years with volatile returns:			\$77		\$51

<sup>7</sup> Hypothetical pension asset return scenario with years of losses (2022 and 2023) and gains (2024 and 2025) relative to market expectations, designed to illustrate the effect of the proposed methodology on pension expense volatility.



10. As demonstrated in the table and graph above, the volatile assumed asset returns drive significant volatility of annual pension cost under the current methodology, while the proposal to smooth asset returns mitigates the associated impact on annual pension cost.
  
11. Regarding the prevalence of asset smoothing, discussed in paragraph 27 of the Petition, PSEG identifies the following 18 organizations as peer companies in its financial statements and proxy disclosures. All 18 organizations sponsor defined benefit pension plans, and 14<sup>8</sup> of the 18 organizations smooth assets, as summarized in the table below.
  
12. When comparing the financial performance of PSEG with these other organizations, the volatility embedded in pension costs for PSEG impairs the comparability of PSEG’s pension costs, cost structure, and overall financial performance to its peers, the majority of whom smooth asset returns for this purpose. Since nearly all of these peer companies are regulated utilities, most of whom use GAAP expense as the basis for rate recovery in the states in which they operate, rate recovery for these utility peers will commonly be based on the less volatile measure of pension expense, with customers benefitting from the more stable cost profile related to pensions.

<sup>8</sup> Based on Aon analysis and research of 10-k filings of PSEG peer companies.

<b>Company</b>	<b>Smooth Assets?</b>
Ameren	Yes
American Electric Power	Yes
CMS	Yes
ConEd	Yes
Dominion	Yes
DTE	Yes
Duke	Yes
Entergy	Yes
Xcel	Yes
Exelon	Yes
PPL	Yes
Sempra	Yes
Southern Company	Yes
Centerpoint	No
Edison International	No
Eversource	No
First Energy	No
WEC Energy	Yes

13. This completes my statement at this time. I reserve the right to submit an additional statement if necessary.

By: Joseph McDonald

Joseph McDonald  
Senior Partner, Aon

Sworn and subscribed before me  
this 1<sup>st</sup> day of September, 2022

*Caitlyn M. White*

CATLYN M. WHITE  
NOTARY PUBLIC OF NEW JERSEY  
My Commission Expires 9/19/2024