December 15, 2010

Technical Director  
Technical Reference No. 1850-100  
Financial Accounting Standards Board  
401 Merritt 7  
PO Box 5116  
Norwalk CT, 06856-5116

Dear Board Members,

Xcel Energy (or “the Company”) respectfully submits its comments on the Financial Accounting Standards Board’s Proposed Accounting Standards Update, Leases – Topic 840 (“the Proposed Standard”). Xcel Energy is a major U.S. integrated electric and natural gas holding company, with annual 2009 revenues of $9.6 billion. Based in Minneapolis, Minnesota, the Company’s operations include the activities of four wholly owned utility subsidiaries that provide electric and natural gas service to approximately 3.4 million electric and 1.9 million natural gas customers in eight states. These utility subsidiaries are NSP-Minnesota, NSP-Wisconsin, Public Service Company of Colorado, and Southwestern Public Service Company, serving customers in portions of Colorado, Michigan, Minnesota, New Mexico, North Dakota, South Dakota, Texas, and Wisconsin.

Xcel Energy is supportive of the joint efforts of the Financial Accounting Standards Board and the International Accounting Standards Board (the Boards) toward lease accounting convergence and development of an accounting standard that improves the recognition and disclosure of the rights and obligations arising under leasing arrangements. However, Xcel Energy feels that certain provisions and applicability of the Proposed Standard should be reconsidered or clarified, and the Company appreciates the opportunity to provide comments on such items.

Xcel Energy would especially like to highlight types of commodity supply arrangements that are widely used in the utility industry, and make clear that these arrangements may be significantly impacted by the final converged leasing standard. Historically, Xcel Energy has accounted for these commodity supply agreements, or purchase power agreements (PPAs), as either an executory contracts or operating leases. The distinction between the classifications of these agreements has not been of significant importance as they are accounted for in a similar manner. The Proposed Standard would significantly impact Xcel Energy in a number of areas including: short-term leases, distinguishing leases from service contracts, scope, lease term, lease payments and transition. Xcel Energy values this opportunity to support the Boards in their development of a converged leasing standard, and to offer its concerns, recommendations, and requests for clarification in these areas.
Question 3 – Short-term Leases

Do you agree that a lessee or a lessor should account for short-term leases in this way? Why or why not? If not, what alternative approach would you propose and why?

The Proposed Standard requires that all short-term leases be included within the scope of the guidance and eases application burden in that the forecasted cash flows underlying the right-of-use assets and liabilities for short-term leases need not be discounted.

The Company has concerns when weighing the benefit of application of the Proposed Standard to short-term leases against the recordkeeping and internal control burden that would be required to accurately report the anticipated future payments for short-term rentals as of each balance sheet date, ranging from rental cars for traveling employees, to equipment used for varying durations in power plant and transmission system construction and maintenance projects.

Adding current assets and current liabilities to the balance sheet for short-term leases will not result in significant incremental financial statement usefulness, but may obscure important liquidity ratios, inflating the balance sheet for future payments due under various short-term executory contracts for which the counterparties have yet to perform.

Xcel Energy notes that paragraph 65 of the Proposed Standard allows lessors the option to not recognize assets or liabilities arising from short-term leases, on a lease-by-lease basis. The Company recommends that the Boards consider a similar scope limitation for lessees in the final converged leasing standard.

Question 4(c) – Distinguishing leases

Do you think that the guidance for distinguishing leases from service contracts is sufficient? Why or why not? If not, what additional guidance do you think is necessary and why?

Assuming that the right-of-use model set forth in the Proposed Standard becomes effective, utility entities that procure energy through PPAs will be subject to significantly different accounting requirements for PPAs that are determined under the guidance to convey the right to use a specified asset (contain a lease) than PPAs that do not convey the right to use a specified asset (do not contain a lease).

Under current U.S. GAAP, a lease asset and obligation are only presented on the balance sheet when the underlying lease arrangement meets one or more of the criteria for a capital lease. Therefore, the judgment that an arrangement contains a lease is currently less crucial under U.S. GAAP financial reporting for a sizable population of (operating) leases, because leases that do not qualify as capital leases are accounted for consistent with executory contracts, with no recognition of a lease asset or lease obligation.

Therefore, determination of whether an arrangement conveys the right to use an asset (contains a lease) will be critically important in the implementation of the new leasing standard. The Proposed Standard does not provide incremental clarification for making these (now more crucial) judgments, but carries forward the existing U.S. GAAP guidance contained in ASC 840-10-15. Under the Proposed Standard, the right to control the use of an asset is conveyed when:
B4(c) The entity has the ability or right to operate the asset or direct others to operate the asset in a manner that it determines while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.

B4(d) The entity has the ability or right to control physical access to the underlying asset while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.

B4(e) The entity will obtain all but an insignificant amount of the output or other utility of the asset during the term of the lease, and the price that the entity will pay for the output is neither contractually fixed per unit of output nor equal to the current market price per unit of output as of the time of delivery of the output. If the price that the entity will pay is contractually fixed per unit of output or at the current market price as of the time of delivery of the output, then the entity is paying for a product or service rather than paying for the right to use the underlying asset.

Much of the need for clarification of the scope of the Proposed Standard relates to the ASC 840 guidance reflected in criterion B4(e) above. When pricing is other than either market price at delivery or fixed per unit of output, per ASC 840-10-15 and the Proposed Standard the pricing is indicative of the conveyance of the right to control the use of the asset (in instances when other parties are not expected to take more than a minor portion of the output). Since the guidance in ASC 840-10-15 was issued, the nature of electric markets, transmission systems and distribution networks has evolved from just the delivery of energy to also include capacity, renewable energy credits (RECs), emission allowances, etc. With the evolution of the products and services included in PPAs, there are two particular principles for which Xcel Energy believes further guidance in this area is required:

1) How should the outputs of a lease be determined?

2) How should the fixed price per unit of output principle be applied?

Output

To apply paragraph B4(e), an entity must determine the portion of future payments to the seller that compensate the seller for the purchaser’s use of the asset. Several questions arise, such as how to treat portions of contractual payments relating to executory costs and contingent items, and how to allocate payments in arrangements with other types of deliverables.

For instance, in a typical PPA arrangement, utility entities often make separate payments for generation capacity (subject to adjustment for periods when the seller’s generation facilities are unavailable), volume-based payments for energy and RECs. Payments may also become due under contract provisions for executory cost pass-throughs and contingent items. In return, utility entities typically receive capacity and energy, and often RECs (in the case of PPAs with sellers using renewable-fuel generation facilities).

Xcel Energy urges the Boards to provide additional clarifying guidance for evaluation of what constitutes an output. Specifically, clarification is needed on how to identify the payments in a multiple-element arrangement that relate to use of an asset. The accounting for capacity and RECs provides good illustrations of these complex judgments.
In the utility industry, generating capacity is a commonly traded commodity. It is common for a utility entity to transact in a capacity market without buying or selling any related energy, for instance in order for the buyer to meet its regulatory operating reserve obligations. In many PPAs, payments for capacity are due only when the independent power producer’s facility is available to generate energy for the buyer (as opposed to shut down, generating for another entity, etc.). Though capacity is a marketable separate deliverable in a PPA, the current existing U.S. GAAP lease guidance may be applied such that energy is deemed the only output of a PPA. In this case, a payment for capacity (when assuming future plant generation availability of 100%) may be determined to be virtually fixed and independent of volume-based payments for energy, resulting in an arrangement for which pricing is other than fixed per unit of output or the current market price as of the time of delivery of the output. Again, this interpretation depends on a view that energy is the only output of a PPA, rather than a view that capacity is a marketable separate deliverable. Thus, in many cases, the conclusion as to whether an agreement contains a lease is dependent upon the determination of which items are considered outputs.

There also is currently a lack of authoritative guidance that seems to appropriately address bifurcating payments for energy and payments for capacity from payments for RECs to be delivered to the buyer in a PPA. Without such guidance, it may be difficult to allocate value to these instruments to apply the Boards’ expected upcoming guidance on Emissions Trading Schemes.

Xcel Energy asks that the Boards provide clarification regarding what specific elements are to be considered “outputs” of an agreement when determining whether an agreement should be accounted for as a lease. The Boards might consider output to be defined as distinct if the entity or another entity transacts for an identical or similar service, product, tradable right or financial instrument separately.

**Fixed Price per Unit of Output**

In addition to per unit pricing that fluctuates with the market price at delivery, other types of variability in per unit pricing exist that do not necessarily convey the right to control the use of an asset.

Paragraph B13 of EITF 01-08 *Determining Whether an Arrangement Contains a Lease* states:

> Task Force members generally agreed that the right to use property, plant, or equipment is conveyed in arrangements in which the purchaser has the right or ability to take all or substantially all of the output or other utility that will be produced or generated by the property, plant, or equipment (or, said another way, when other parties will not take more than a minor amount of the output) if the arrangement's pricing contains an element that is designed to recover some or all of the supplier's capital investment in such property, plant, or equipment irrespective of the quantity of output taken by the purchaser.

Certain types of pricing arrangements that are other than fixed or equal to market price at delivery do not pay the seller without regard to variability in output, but rather are designed to charge the buyer a proxy for the market price of the output, or to recover certain variable operating costs of providing output to the purchaser (fuel, maintenance, other executory costs, etc). The principle that price adjustments related to these items should be excluded from the lease element of an arrangement is supported by the U.S. GAAP definition of minimum lease payments, which properly excludes these items, as well as contingent payments.
Xcel Energy encourages the Boards to provide qualitative, principles-based guidance in this area. The fixed price per unit of output criterion is a bright line that does not adequately scope out of lease accounting the full universe of agreements for which the substance is the purchase of a product, service, tradable right or financial instrument, or some combination of these items.

Xcel Energy recommends the Boards utilize a concept similar to that used to qualify contracts for the normal purchase and sale exception of derivative accounting, under which contracts can contain variable terms that are clearly and closely related to 1) producing the output or 2) the market price of the output, without conveying the right to control the assets used to provide the services. For instance, price per unit under a contract for all but a minor portion of the output of a particular plant should be allowed to vary with the operations and maintenance costs to deliver products, or indices and adjustments reflective of those costs, without the arrangement qualifying as a lease. The decision of whether to include such a plant in the consolidated balance sheet of an enterprise should be determined under variable interest entity accounting guidance, not lease accounting.

To establish this qualitative principle in the converged leasing standard, Xcel Energy suggests that paragraph B4(e) be revised as follows:

B4(e) The entity will obtain all but an insignificant amount of the output or other utility of the asset during the term of the contract, and the contract payments are specified in terms of the time that the underlying asset is made available or reserved for the benefit of the entity, rather than in terms of the output from the asset. Indicators that a contract contains the characteristics of the purchase of output include, but are not limited to pricing based on any of the following pricing mechanisms: 1) a fixed price per unit of output, 2) a predetermined formula per unit of output, 3) a formula for units of output based on variable prices of inputs, market prices for the same or similar outputs, or inflationary adjustments, or 4) a current market price as of the time of delivery of the output. In contrast, pricing mechanisms that indicate that a contract contains characteristics of a lease include: 1) pricing based on term (i.e., the passage of time) without regard to quantity of output, or 2) pricing that does not allow for a reduction in payments if the expected output is not achieved or accepted during all or a portion of the term.

Question 5 – Scope Exclusions

Do you agree with the proposed scope of the proposed guidance? Why or why not? If not, what alternative scope would you propose and why?

When the consensus in EITF Issue 01-8 Determining Whether an Arrangement Contains a Lease, was issued in 2003, as codified in ASC 840-10-15, the transition guidance did not require U.S. entities to assess contracts that were executed or acquired prior to the issuance of that consensus. Unless pre-2003 contracts were modified and reassessed subsequent to the adoption of EITF 01-8, these arrangements continue to be commonly accounted for as executory contracts by U.S. entities.

It is Xcel Energy’s understanding that the Boards do not intend for the converged leasing accounting requirements to change this scope of lease accounting, but rather to improve recognition, measurement, and disclosure of contracts already subject to existing lease accounting guidance.

Xcel Energy proposes that the Boards not change this scope of lease accounting, and carry forward transition guidance consistent with current U.S. GAAP, such that the standard need only be applied to contracts entered into or acquired after the beginning of the first reporting period following the issuance of EITF 01-8 on May 28, 2003.
Question 8 – Lease Term

Do you agree that a lessee or a lessor should determine the lease term as the longest possible term that is more likely than not to occur taking into account the effect of any options to extend or terminate the lease? Why or why not? If not, how do you propose that a lessee or a lessor should determine the lease term and why?

Xcel Energy believes that only the lease term to which the parties are contractually obligated should be reflected in the rights and obligations recognized in connection with a lease agreement. Since the lessee is not committed to make payments beyond the original lease term, no obligation exists for periods subsequent to the initial contractual term.

Consistent with the concepts illustrated in BC7(b) of the Proposed Standard, which addresses concerns regarding the right-of-use model, until a term-extending option is exercised by the lessee, the lessee lacks the unconditional right to use the underlying asset and, therefore, an unconditional liability to make lease payments for periods subsequent to the initial contractual term.

Also, in an arms length transaction, the value of any option(s) for an additional lease term(s) is built into the lease payments to be made during the initial contractual term, and therefore would be included in the right-of-use asset calculated based on the payments for the initial contractual term of the lease.

Question 9 – Lease Payments

Do you agree that contingent rentals and expected payments under term option penalties and residual value guarantees that are specified in the lease should be included in the measurement of assets and liabilities arising from a lease using an expected outcome technique? Why or why not? If not, how do you propose that a lessee should account for contingent rentals and expected payments under term option penalties and residual value guarantees and why?

Xcel Energy has entered into approximately 170 PPAs with sellers using renewable-fuel generation facilities (wind and solar power) for which Xcel Energy is committed to pay the sellers only when the facilities produce energy. While the sellers and the Company model and estimate the expected production of energy initially and during the term of the PPAs, actual production will always differ from those estimates.

As the Company makes payments for these PPAs only when energy is produced, assuming these arrangements qualify as leases under the Proposed Standard, the right-of-use assets and liabilities could be significantly impacted by abnormal weather patterns, unplanned outages, maintenance and the seller’s operating polices.

Under the Proposed Standard, the Company would need to reassess, on a quarterly basis, the carrying amount of the liability to make lease payments, to determine if there was a significant change in the liability since the previous reporting period. Changes in the expected amount of such payments would be recorded in earnings to the extent that those payments relate to current or prior periods (consistent with the Company’s current expense recognition practice), or as an adjustment to the right-of-use asset and liability to the extent that those changes relate to future periods.
Recording right-of-use assets and liabilities based on estimated payments that are contingent on future events would not accurately reflect the obligations of the Company. Further, it is not possible to accurately forecast actual energy purchases that will be recorded in the future for these arrangements. Additionally, these payments are for energy, not to compensate the owner for the Company’s “use” of the generating facility.

Any financial statement user benefit of recording right-of-use assets and liabilities based on estimates of future payments for energy for which the Company is only contingently obligated does not outweigh the expense of recordkeeping and internal control burden that will be required to report anticipated contingent energy payments initially and on an ongoing basis.

The Company suggests that a right-of-use asset and liability be measured only once at inception of a lease, and to be based on the minimum lease payments for which the lessee is contractually obligated, consistent with the current U.S. GAAP accounting for capital leases. The Company also reiterates its recommendation that the Boards provide clarification regarding what specific elements are to be considered “outputs” of an agreement when determining whether the agreement should be accounted for as a lease.

**Question 16 - Transition**

(b) Do you think full retrospective application of lease accounting requirements should be permitted? Why or why not?
(c) Are there any additional transition issues the boards need to consider? If yes, which ones and why?

Xcel Energy believes that a full retrospective application of the lease accounting requirements should be permitted, as it would achieve comparability across all periods presented by an entity subsequent to implementation. It would also, for example, accurately present the economics of a 20-year lease in the last five years of the term versus a new five year lease.

However, the process of analyzing only the remaining terms of an entity’s lease arrangements as of the date of initial application, as set forth in the proposed simplified retrospective approach, has practical benefits to entities with many or complex leases. Therefore, Xcel Energy recommends that entities be given the ability to choose between the simplified retrospective approach and the full retrospective approach at transition, on a lease by lease basis.

This concludes Xcel Energy’s comments on the Proposed Standard. The Company hopes that the Boards find the Company’s concerns, recommendations, and requests for clarification useful in their efforts to develop a final converged leasing standard. Xcel Energy again thanks the Boards for the opportunity to comment on this critical change to authoritative accounting standards.

Sincerely Yours,

Teresa S. Madden  
Vice President and Controller  
Xcel Energy Inc.