Minnesota Public Utilities Commission

Staff Briefing Papers

Meeting Date: May 1**,** 2014..*Agenda Item # **2**

Company: Northern States Power Company d/b/a Xcel Energy

Docket No. E,G-002/D-12-151

In the Matter of Northern States Power Company's Request for Approval of the Annual Review of Remaining Lives Depreciation for Electric and Gas Production and Gas Storage Facilities and Net Salvage Rates for 2012

Issue(s): Should the Commission approve the proposed depreciation lives as modified in the August 6, 2012 reply comments?

Staff: Jerry Dasinger ....(651) 201-2235

Relevant Documents

Xcel Filing...February 17, 2012
Department Comments ....June 27, 2012
Xcel Reply Comments...August 6, 2012[1]
Department Response Comments .... August 17, 2012
Xcel supplemental Information .... October 26 & 29, 2012

The attached materials are workpapers of the Commission Staff. They are intended for use by the Public Utilities Commission and are based upon information already in the record unless otherwise noted.

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[1] The reply comments are dated August 6, 2012 but are shown as received by edockets on August 7, 2012.

Statement of the Issue

Should the Commission approve the proposed depreciation lives as modified in the August 6, 2012 reply comments?

Background

On February 17, 2012, Xcel filed its 2012 Review of remaining lives.

On June 27, 2012, the Department filed comments recommending limited approval with modification and requested that Xcel provide additional information.

On August 6, 2012, Xcel filed reply comments offering an alternative proposal in response to Department concerns and provided additional information.

On August 17, 2012, the Department filed response comments recommending approval of Xcel's revised proposals.

On October 26, 2012, Xcel filed supplemental information providing an update of the costs related to a life extension for the Granite City plant.

Party Positions

A. Depreciation Lives

Xcel Filing

Xcel stated that this Petition provides recommendations stemming from its annual review of electric and gas production and gas storage asset lives and net salvage rates as of January 1, 2012. The review evaluated system demand, availability of fuel supplies, operating and maintenance costs, and future technological advancements that influence the decision about retiring electric and natural gas facilities. Overall, this Petition reflects a decrease in depreciation expense of $477,668[2] based on beginning of year balances for assets not presently included in rate riders. The Company requested that the new remaining lives and net salvage rates become effective January 1, 2012.

According to the Company no new production plants are expected to go into service in 2012. To begin its analysis of 2012 lives, the Company made a one-year passage of time adjustment to the certified remaining lives of all facilities. Subtracting one year from the present certified

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[2] This amount does not include the impact of the decrease in depreciation resulting from the remaining life changes for High Bridge and Riverside that are reflected in the settlement agreement in the 10-971 electric rate case. The resulting overall impact including those changes would be an additional decrease in annual depreciation expense of $6,393,440.

remaining life results in the proposed remaining life as of January 1, 2012. The passage of time adjustment does not cause a change in the annual depreciation accrual. This adjustment merely reflects that Xcel Energy production facilities have aged one year since January 1, 2011. Attachment B of the filing shows the Comparison of Present and Proposed Lives, as it relates to depreciation expense.

In addition to the assumed passage-of-time adjustment in lives of all plants, Xcel requested life changes to:

• Blue Lake Units 1 through 4 other production plant,
• Granite City other production plant, and
• Key City other production plant.

Xcel stated those three plants had a remaining life of 1 year as of January 1, 2012. All three have minimal use but continue to provide value to the system so Xcel plans to continue using the plants for six years. Xcel requested approval of a five year life extension for the plants. The proposed increase to the remaining life would decrease depreciation expense $1.09 million, $850,000, and $531,000 respectively.

Department Comments

The Department recommended that the Commission approve Xcel's proposed service lives, salvage rates, and resulting depreciation rates effective January 1, 2012 for plant in service, except for those related to Blue Lake Units 1 thru 4, Granite City, and Key City.

The Department stated it has three concerns with Xcel's justification for the proposed Blue Lake life extension. First, the Department is concerned that Xcel indicated in its response to the Department's information request in the most recent rate case (10-971) that the Company planned only to extend the lives of its Black Dog and Prairie Island plants in the next two years, but then proposed to extend the life of Blue Lake Units 1 through 4 and other generation facilities in this depreciation petition. This practice results in higher depreciation expense being collected through rates determined in the rate case, but lower depreciation expense recorded for accounting purposes, which can result in an over recovery of costs.

Second, the Department noted that generally capital additions are the main reason for increasing the life of an asset or plant; however, Xcel has not provided support for any capital additions for the Blue Lake Units 1 through 4 that support the life extension proposed by Xcel in this petition.

Third, the justification Xcel provided in its response to an Information Request is flawed. Xcel indicated that with the loss of production of Sherco 3 due to a fire and the delay of the proposed new unit at Black Dog, small peaking plants like Blue Lake are needed to ensure system reliability for customers. However, the Department notes that the Sherco 3 and Black Dog units are considered baseload units, while Blue Lake Units 1 through 4 are old peaking units; therefore, these are not interchangeable units for energy production purposes since baseload and peaking units serve different functions.

The Department noted that the remaining life established for accounting purposes does not limit Xcel's ability to operate a plant that is nearly or fully depreciated. That is, just because Xcel has recovered the costs of a generation plant for ratemaking and accounting purposes does not require stopping the operation of the plant if the plant continues to be useful and needed. The Department concluded that Xcel's assertions that energy needs due to situations concerning Sherco 3 and Black Dog support a proposed life extension for Blue Lake are flawed.

The Department recommended that the Commission deny Xcel's request to extend the remaining life of the Blue Lake Units 1 to 4.

The Company proposed to extend the remaining life of the Granite City peaking plant from one year to six years as of January 1, 2012. The Department noted the same concerns with the proposed Granite City life extension as discussed above for Blue Lake. Further, the Department noted that Xcel's December 1, 2011 "Resource Plan Update" in Docket No. E-002/RP-10-825 indicates that the Company plans to retire the Granite City plant in 2013. This update was filed after the Sherco 3 incident and also indicated Xcel's intent to withdraw the Black Dog CN. The estimated impact to total Company depreciation expense for this proposed change is an annual decrease of $850,000. Therefore, the Department recommended that the Commission deny Xcel's request to extend the remaining life of the Granite City peaking plant.

The Company proposed to extend the remaining life of Key City peaking plant from one year to six years as of January 1, 2012. The Department noted the same concerns with the Key City life extension as were discussed above for Blue Lake. Further, the Department noted that Xcel's December 1, 2011 "Resource Plan Update" in Docket No. E-002/RP-10-825 indicates that the Company plans to retire the Key City plant in 2013. The estimated impact of this change to total Company depreciation expense is an annual decrease of $450,000.[3] Therefore, the Department recommended that the Commission deny Xcel's request to extend the remaining life of the Key City peaking plant.

Xcel Reply

Xcel stated its response to DOC Information Request 159 submitted February 1, 2011 in its rate case, indicated that the Company's February 2011 annual remaining lives filing would propose extensions for Black Dog Units 3 and 4 and Sherco Units 1 and 2, consistent with what it presented in the rate case and the information known at that time. In that response the Company also indicated the possibility that through the annual review process for 2012, new information could support life extensions that may be proposed in the February 2012 annual remaining lives filing.

The recommended life changes for Blue Lake Units 1-4, Granite City, and Key City reasonably reflected the best available information at the time the 2012 remaining life assessment was completed in February of 2012. However, to resolve the issues in this proceeding, Xcel proposed

[3] Page 6 of the Company's filing shoes this as $531,000.

to withdraw its request to extend the lives of these plants. As a result of this withdrawal, the decrease to depreciation expense in 2012 related to these plants that was proposed in the original Petition will be eliminated, and these units will be fully depreciated at the end of 2012.

Xcel stated that these plants will continue to be part of the MISO reserve and it does not plan to retire them from operations at the end of 2012. However, there will be no depreciable life after 2012 and it does not expect any capital additions will be required to continue operating these plants. The Company expects all work on the plants to maintain them in their current state will be handled through maintenance.

Xcel requested that the Commission approve:

- The proposed service lives, salvage rates, and resulting depreciation rates effective January 1, 2012 as proposed in its original Petition, except for the proposed life extensions for the Blue Lake Units 1-4, Granite City, and Key City peaking plants, and the salvage rate for the Minnesota Valley plant.
- Its request to withdraw the life extensions for Blue Lake Units 1-4, Granite City, and Key City proposed in our original Petition;

Department Response

The Department noted that the Company’s withdrawal request is consistent with the Department’s recommendation not to extend the lives of these plants.

Xcel Supplemental Information

The Company stated that Energy Supply recently updated its plans for the Granite City plant and concluded that additional work will be needed to continue operations through 2018. Specifically, a new operating control system for Units 1 and 2 is required at an estimated cost of $294,000. The existing control system is obsolete and no longer supported by the manufacturer. If the system is not replaced, control cards could fail, resulting in outages. In addition, Xcel stated it expects it will be necessary to replace the diesel starting motors at the Granite City plant in 2016 at a cost of approximately $600,000.

B. Gas Storage Westcott Compressor Equipment

Xcel Filing

Xcel also requested a life change for the Wescott gas storage plant. The Company stated that the Wescott LNG Plant is a liquefied natural gas plant placed in-service in 1972. The plant cools then stores the liquefied natural gas in large storage tanks. Vaporizing equipment is used later to warm and convert the liquefied methane back to a gas for use in the distribution system. In past years, the remaining life that is used for the structures and improvements account for both the Wescott Production Plant and the Wescott LNG Plant has been the same as these facilities would likely be retired from service simultaneously. However, the Wescott LNG Plant is unique in that there is separate identifiable systems within the plant that function independently from other systems, thereby allowing for the possibility of having different remaining lives for each system. For that reason, the life used for the structure and improvement account does not necessarily need to match the life of other equipment. Presently all systems have a remaining life of 6 years, as of January 1, 2012, except for the vaporizing equipment. The vaporizing equipment currently has a remaining life of 16 years. The Company stated it is currently in the process of replacing the refrigerated compressor unit at the Wescott LNG Plant. It is expected that this project will be completed sometime in the second quarter of 2012. The forecasted capitalized value of this replacement is approximately $14.5 million dollars.

Due to the upgrade and replacement of this refrigerated compressor unit, Xcel proposed to increase the remaining life for the Compressor Equipment account, FERC Account 363.3. Currently this account has a remaining life of 6 years. The Company requested a 14-year lengthening of the remaining life out to 20 years. Due to the size of the addition in comparison to the current plant balance of the account itself, the forecasted capitalized amount of the new compressor unit is included separately on Schedule B. The new addition will result in an increase in depreciation of approximately $355,000, assuming an in-service date of July 1, 2012. The change in remaining life produces a decrease to annual expense of approximately $20,000 for the current plant balance of the Compressor Equipment account. The total change in depreciation for 2012 is an increase of approximately $335,000.

Department Comments

According to the Department, the Company stated that it is currently in the process of replacing the refrigerated compressor unit at the Wescott LNG Plant at a cost of approximately $14.5 million. Due to the replacement of the unit, Xcel proposed to increase the remaining life for the compressor equipment account from 6 years to 20 years effective January 1, 2012.

The Department noted that in Docket E-002/PA-11-902 the Company had submitted a replacement options cost-benefit analysis. The Company's analysis indicated that replacing the unit with a gas turbine-driven compressor was the most cost-effective solution.

The Department recommended the Commission approve the Company's request to increase the remaining life of the Gas Storage Westcott Compressor Equipment account from 6 years to 20 years.

C. Minnesota Valley Steam Production Plant and Dam

Xcel Filing

Xcel proposed one change to the net salvage rate for the Minnesota Valley steam production plant. The Minnesota Valley Plant is a former Steam Production facility located in Granite Falls, Minnesota along the Minnesota River. Minnesota Valley last burned coal in 2004, and the air permit was formally retired in 2009.

According to the Company, while the plant is no longer in operation, it has yet to be retired or demolished and is still being depreciated in order to collect the 2009 estimated cost of decommissioning the plant of $13,874,964. This treatment was initially ordered by the Commission in its August 26, 2005 Order in the Company's 2005 Remaining Life proceeding.[4]

Xcel updated its estimate for the demolition, decommissioning, and abatement of the entire facility based on quotes received from outside contractors who had specialized experience with that type of work. The new estimate is $18,757,000.

In addition to the demolition, remediation and decommissioning of Minnesota Valley plant facilities, the Company stated it must also remove the Minnesota Falls Dam.

Based on the cost estimates for removal of the Minnesota Valley steam production plant, as well as the dam, Xcel Energy is proposing a change of net salvage rate from -101.9% to -169.0%. This change in net salvage rate produces an increase to annual expense of $1.66 million.

Department Comments

Demolition, Decommissioning and Abatement at Minnesota Valley

The Department stated that the Minnesota Valley Plant is no longer in operation but is still being depreciated in order to collect the cost of decommissioning. In 2011, Xcel requested new budgetary quotes from four outside contractors to perform the demolition, remediation and decommissioning work at the Minnesota Valley Plant.

The Department asked the Company in Information Request No. 3 (attached to the DOC comments) the following:

- Please provide copies of quotes from the four contractors and fully explain how they compare to the total estimate;
- Please explain how contractor will be selected; and
- Please provide schedule for when work will occur and be completed.

The Company's response showed contractor quotes for three scopes of work: asbestos abatement, demolition with scrap credit, and site work. The remaining five scopes of work - oversight and administrative, contingency, escalation, coal yard closure and hazardous material abatement - were estimates of the Company. Based on its review of the contractor quotes provided by the Company, the Department stated it considers the quotes for asbestos abatement, demolition with scrap credit, and site work to be reasonable estimates.

The Department also reviewed the remaining estimates provided by the Company. Based on its review, the Department noted that the contingency cost category estimate of $2,651,000, and the

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[4] E,G-002/D-05-288

escalation cost category estimate of $2,476,000 together comprise 27 percent of the total estimate of $18,757,000, which is quite high.

The Department stated it does not believe that the Company's explanation contained in its IR response provides sufficient support for the escalation and contingency cost categories to comprise 27 percent of the total cost estimate for Minnesota Valley Plant decommissioning. Therefore, the Department requested that the Company provide additional information in its reply comments to support these cost estimates.

Dam Removal

According to the Company, inspections identified several potential structural deficiencies within the aging structure. The Company stated that removal of the dam was determined to be the most cost-effective option to address the deficiencies.

In response to a Department IR, Xcel stated:

> We note that since our remaining lives petition was submitted we have received an offer from an entity to take ownership of the dam. As part of the proposal, the Company would pay the entity a trade secret amount of money[5] and the entity would undertake ongoing responsibility for the long-term plan to remove, repair or otherwise modify the dam to ensure its safe operation. We have accepted this proposal, it will be less costly than if the Company were to remove the dam. However, an agreement must still be finalized.

Based on its review, the Department recommended that the Company provide in its reply comments an update on the status of the sale of the Minnesota Falls Dam. Additionally, in reply comments Xcel should provide the updated net salvage rate for the Minnesota Valley Plant and the corresponding change in depreciation expense to reflect the sale of the Minnesota Falls Dam.

Xcel Reply

The Company stated that its current Petition requested approval of a revised net salvage rate to reflect updated removal costs, including the costs to demolish the Minnesota Falls dam, to be recovered over the remaining life of the plant. This would result in an increase of $1,660,619 in depreciation expense.

Xcel stated that while it continues to support the updated removal cost estimates, to eliminate the continuation of depreciation expense for this retired asset after 2012, it proposed to use the accumulated depreciation reserve balance to fully depreciate Minnesota Valley by the end of 2012 and reallocate the depreciation expense across each FERC Account for steam production. Specifically, it proposed to reallocate the 2012 year-end accumulated depreciation reserve balances among the individual units in steam production by FERC Account, such that as of the

[5] The specific amount is found on page 13 of the Department trade secret version of their comments.

beginning of 2013, the Minnesota Valley steam plant reserve balance will equate to the sum of both the plant balance and the most recent remaining cost estimate for demolition and dismantlement of $21,034,000.

Using the current approved remaining life and net salvage rate for Minnesota Valley, the net book value is negative $8,135,823. For Minnesota Valley to be fully depreciated at the end of 2012, the net book value needs to be a negative $21,034,000. To resolve the deficit of $12,898,177 ($21,034,000 - $8,135,823), the Company proposed to transfer reserve from the operating steam plants to Minnesota Valley. As a result of this reallocation, the Minnesota Valley plant will be fully depreciated as of the beginning of 2013

In its response to the DOC's request for additional information to support the escalation and contingency components of these costs, the Company noted that in reviewing its Petition it discovered an inadvertent error in the calculation of the escalation amount. Correcting the calculation provides an escalation estimate of $653,000 as compared to its original calculation of $2,476,000. Xcel stated it estimated the escalation cost component by assessing a 5 percent annual increase to the estimated costs based on when the costs are expected to occur within the decommissioning project schedule.

In determining the contingency component, it added an increase of 15 percent to the majority of the cost components, certain minor items were not included in the escalation calculation, and certain specific contingency costs were added based on previous project experience. The 15 percent contingency is consistent with the demolition and dismantling cost study performed by TLG Services, Inc. in 2009.

Xcel stated that throughout the notification periods regarding the condition of the dam, it had been contacted by various entities regarding the possibility of taking ownership of the dam. These entities included local government entities as well as local businesses. In general, there was an interest in maintaining the dam and the water level as it currently stands, both for business purposes and for recreation purposes. However, nothing substantive resulted until late April 2012, when the Company executed a letter of intent from Granite Falls Energy LLC (GFE), to transfer ownership of the dam. However, on June 21, 2012, the Company received a letter from GFE stating its desire to stop its efforts to obtain ownership of the dam. As a result, the Company will continue with the dam removal, implementing the least cost approach to meet DNR requirements.

Xcel requested that the Commission approve:

- Its request to withdraw the net salvage rate for the Minnesota Valley Plant proposed in its original Petition; and
- Reallocation of the 2012 year-end accumulated depreciation reserve balances among the individual units in steam production by FERC Account such that the Minnesota Valley plant, including the updated removal costs proposed in its original Petition, is fully depreciated by the end of 2012.

Department Response Comments

The Department noted that the treatment by Xcel of the reallocation of the reserve within the steam production plants is generally the same as if there were a gain on sale of a facility that was recorded to the reserve. The Department stated it considers Xcel's proposal to reallocate the $12.9 million deficit among the steam production plant accounts to be reasonable since it is the same type and function of production plant. Basically, this treatment would allow Xcel to collect the unrecovered removal and demolition costs for the Minnesota Valley Plant over the future life of other related steam plants.

However, the Department stated it is concerned that only about 40 percent of the removal and demolition costs for Minnesota Valley Plant was collected over the life of the plant, with the remaining 60 percent to be recovered after the plant is no longer operating. The Department asks Xcel to be prepared to explain why this result occurred and what Xcel will do to ensure that such an occurrence does not happen with other plants.

The Department is also concerned that theoretically the 15 percent contingency cost built into the Minnesota Valley Plant removal and demolition is rather high; however, the Department is less concerned about this issue because of the true-up to actual costs that will occur when removal of this plant is completed and recovered in the reserve - Account 108, Accumulated Provision for Depreciation of Electric Utility Plant. Thus, the DOC recommended approval of the Company's revised proposals with the requirement that Xcel provide a compliance item in Xcel's future Depreciation Study filing when the final retirement is completed. The compliance filing should include information regarding a comparison of estimated retirement costs (including cost of removal, demolition costs, salvage, etc.) to actual retirement costs, and the final accounting for the Minnesota Valley Plant retirement.

D. Sherco 3

Xcel Filing

According to Xcel, at the time of the failure there were several major projects which had been completed during the scheduled overhaul which were waiting to be in-serviced. These projects have a value of approximately $23 million. These projects were not damaged by the failure, and will be ready for use once Unit 3 comes back on-line. The Company stated it in-serviced these projects into a Held for Future Use account. While in Held for Future Use the projects will be included in rate base, but will not be depreciated. Once Unit 3 is back in-service, the projects will begin depreciation using the approved remaining life for Sherco 3 at the time.

Department Comments

In response to a DOC IR regarding several major projects which had been completed during the scheduled overhaul, the Company replied that all of the $23 million relates to Sherco Unit 3. The amount reflects installation of equipment to replace various Sherco Unit 3 turbine sections with a more efficient design and to increase steam flow allowing a 20 to 40-megawatt (MW) increase of rating capacity.

The Company stated in its response that the major projects for Sherco 3 were completed in November 2011. The Department requested that Xcel provide in its reply comments information to show that these major project additions (of approximately $23 million) for Sherco 3 were included and approved in current rates for the 2011 test year, and what proportion of these costs were included as a plant addition to rate base and related depreciation expense.

Xcel Reply Comments

Xcel stated that the Department requested it provide additional information on the Sherco Unit 3 additions of $23 million identified in its Petition including a confirmation that these assets were approved as a part of the 2011 test year rate case in Docket No. E002/GR-10-971. The identified Sherco Unit 3 projects were part of the uprate project to increase plant capacity. These projects had been completed at the time Sherco Unit 3 experienced a failure in November of 2011.

The costs associated with the project were placed into a Held for Future Use (HFU) Account. Xcel confirmed that these projects were included and approved in current rates for the 2011 test year. Attachment 3 of the reply provided the proportion of these costs that were included as plant additions to rate base and related depreciation expense as well as the 2011 test year revenue requirements associated with these capital additions.

Xcel stated that in its Petition, it noted that none of these projects were damaged in the November 2011 event; however, the Company has since learned that a portion of the projects were damaged. This does not affect the accounting treatment of these costs, as the current restoration of these assets is being covered by insurance and the entire project will be placed in service as expected once Sherco Unit 3 comes back on line.

Department Response Comments

The Department stated that Xcel provided in its Reply Comments the additional information that it requested related to the 2011 capital investment at Sherco 3 and associated rate treatment. Based on its review of additional data provided by Xcel, the Department stated it has no further concerns on this matter and appreciates Xcel's response.

E. Filing Requirements

Xcel

The Company stated that the Commission's September 8 Order in docket 11-144 requires it to provide:

- An explanation and schedule of the differences between depreciation remaining lives and

Integrated Resource Plan planning lives of electric production plants. This information was provided in Attachment F.

- An attachment providing a history of the last time a change occurred to either the estimated life or salvage value estimate of our production facilities. This information was provided in Attachment H.

Department

Based on its review of Attachment F, the Department stated it considers Xcel explanations for the differences between the depreciation life and the IRP planning life to be reasonable at this time.

The Department stated that in this filing, Xcel provided in Attachment H a historical comparison of changes to remaining lives and net salvage rates. This attachment is a useful reference, providing, for example, the docket numbers in which changes in lives or salvage values occurred, to allow for further background into why such changes occurred. The Department concluded that Xcel has complied with Commission's 2011 Depreciation Study Order.

The Department recommended that the Commission require Xcel to continue to provide the information in Attachments F and H in future depreciation studies.

F. Pending Rate Case Settlements

Xcel

Xcel stated that part of the settlement agreement in Docket 10-971 calls for adjustments to depreciation expense, resulting from extensions in the remaining lives for the Riverside and High Bridge power plants.

The remaining life for Riverside is 27.2 years as of January 1, 2012. The 10-year lengthening of remaining life proposed for Riverside in the settlement agreement would increase the remaining life to 37.2 years. This change in remaining life produces a decrease to annual expense of $2.63 million.

The 10-year lengthening of remaining life for High Bridge proposed in the settlement agreement would increase the remaining life to 36.4 years. This change in remaining life produces a decrease to annual expense of $3.76 million.

Department

The Department stated that in its May 14, 2012 Order in Docket No. E002/GR-10-971, the Commission approved the settlement agreement submitted by the Company in the electric rate case. Part of the settlement agreement included adjustments to decrease the depreciation expense because of the extensions in the remaining lives of the Riverside and High Bridge power plants.

Based on its review, the Department confirmed that the Company has reconciled its calculation for the annual decrease of depreciation expense established in the settlement agreement with the decrease proposed in the instant docket resulting from the remaining lives extension for the Riverside and High Bridge Power Plants.

Staff Analysis

Life Extension for Three Plants

In this filing Xcel requested approval to extend the lives of three plants that had a remaining life of one year as of January 1, 2012: Blue Lake Units 1 through 4 other production plant, Granite City other production plant, and the Key City other production plant.

The proposed increase to the remaining life would decrease depreciation $1.09 million, $850,000 and $531,000 for each of the plants respectively.

The Department recommended that the Commission deny Xcel's request to extend the remaining life of the three plants.

To resolve the issues in this proceeding, Xcel proposed to withdraw its request to extend the lives of these plants.

Staff believes Xcel request to withdraw the proposal is the only equitable resolution to the issue. The Company's most recent general rate case preceding this filing was Docket No. E-002/GR-10-971. The test year in that rate case was 2011 and included a 2012 step-in for some costs related to the Monticello LCM/EPU. The test year in that rate case included one full year of depreciation expense for the three plants based on the existing life which would end in 2012. The test year expense would have been the same or close to the 2012 expense of $2,965,200.[6] The rates set in that rate case recovered that amount annually for as long as they were in effect.

The next rate case filed by Xcel was Docket No. E-002/GR-12-961. The test year in that case was 2013. Therefore, the rates from the 10-971rate case were in effect only for 2011 and 2012. The rates set in the 10-971 rate case recovered the total depreciation expense for the final year remaining life for the plants in 2012. If the Company's proposal were adopted, for financial accounting purposes the Company would have recorded only one sixth of the final year of expense in 2012 and Xcel's plant accounts would have reflected that. The plant balances on Xcel's books are the starting point in determining the rate base in a rate case. Under those circumstances, when Xcel filed the 12-961 rate case it would have included one sixth of the depreciation expense which had already been recovered from rate payers in 2012. This would

[6] The decrease in depreciation expense for under Xcel's proposal of $2,471,000 for all three plants would be 5/6 of the total remaining depreciation for the plants.

have resulted in a double recovery of five sixths of the 2012 depreciation expense.

Depreciation, like other test expenses are not trued up between rate cases. However, because depreciation is based on a capitalized cost adjustments that affect the remaining balance can result in double recovery. Therefore, care must be taken when changing depreciation lives.

The Department stated it is concerned that only about 40 percent of the removal and demolition costs for Minnesota Valley Plant was collected over the life of the plant, with the remaining 60 percent to be recovered after the plant is no longer operating. The Department asks Xcel to be prepared to explain why this result occurred and what Xcel will do to ensure that such an occurrence does not happen with other plants. The Company did not respond to this request in its written comments. Therefore Staff suggests that the Commission require a response in a compliance filing.

Sherco 3

On page 11 of its initial filing, Xcel stated, regarding the $23 million of Sherco 3 plant additions: While in Held for Future Use the projects will be included in rate base, but will not be depreciated.

On page of its August 6, 2013 reply, Xcel stated:

> We placed the costs associated with the project into a Held for Future Use (HFU) Account. We confirm that these projects were included and approved in current rates for our 2011 test year and provide as Attachment 3 the proportion of these costs that were included as plant additions to rate base and related depreciation expense as well as the 2011 test year revenue requirements associated with these capital additions.

Attachment 3 has a column for the 2011 test year and a column for 2011 actual. Based on that schedule, it appears that Xcel didn't record depreciation expense for the 2011 actual but did include depreciation expense for purposes of rate recovery. This contradicts its explanation of how these costs were included in the rate case. Because the plant was not placed into service until late 2013, depreciation should not have started until that time.

Other

The Department recommended that Xcel be required to file its next annual remaining lives update for electric and gas production and gas storage facilities on February 18, 2013. Xcel filed its 2013 filing as an update to this filing on October 1, 2013. Because the update was the 2013 filing, it was assigned a new docket number, E,G-002/D-13-1158. For that reason, the recommendation is not included as a decision alternative.

Decision Alternatives

Service lives, salvage rates, and resulting depreciation rate

1. Approve Xcel's proposed service lives, salvage rates, and resulting depreciation rate effective January 1, 2012 for plants in service as revised in its August 6, 2012 Reply Comments and its request to withdraw the life extensions for Blue Lake Units 1-4, Granite City, and Key City proposed in its original Petition. (Xcel, DOC)

2. Approve Xcel's proposed service lives, salvage rates, and resulting depreciation rate effective January 1, 2012 for plants in service as initially filed.

3. Do not approve Xcel's proposed service lives, salvage rates, and resulting depreciation rate.

Reallocation of the 2012 year-end accumulated depreciation reserve balances for Minnesota Valley

4. Approve the reallocation of the 2012 year-end accumulated depreciation reserve balances among the individual units in steam production by FERC Account such that the Minnesota Valley plant, including the updated removal costs proposed in its original Petition, is fully depreciated by the end of 2012 and allow Xcel to withdraw it request for the net salvage rate change for the Minnesota Valley Plant proposed in its original Petition. (Xcel, DOC)

5. Do not approve the reallocation of reserves.

Accumulation of removal and demolition costs

6. Require that Xcel provide an explanation within 30 days of the order in this docket as to why only about 40 percent of the removal and demolition costs for Minnesota Valley Plant was collected over the life of the plant, with the remaining 60 percent to be recovered after the plant is no longer operating, and to explain what Xcel will do to ensure this does not occur with other plants. (DOC)

7. Do not require an explanation.

Future Filings

8. Require Xcel to continue to provide in future depreciation studies an explanation and schedule of the differences between the depreciation remaining lives and Integrated Resource Planning lives of electric production plant. (Xcel, DOC)

9. Require Xcel to continue to provide in future depreciation studies a historical comparison of changes in remaining lives and net salvage rates. (Xcel, DOC)

10. Require Xcel to file its next five-year depreciation study and net salvage rate study for electric and gas production and gas storage facilities on February 17, 2015. (DOC)

11. Require Xcel to provide a compliance item in Xcel's Depreciation Study when final retirement is completed for the Minnesota Valley Plant. The compliance filing should include information regarding a comparison of estimated retirement costs (including cost of removal, demolition costs, salvage, etc.) to actual retirement costs, and the final accounting for the Minnesota Valley retirement. (DOC)

Recommendation

Staff recommends 1, 4, 6, 8, 9, 10 and 11