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August 28, 2019

Daniel P. Wolf
Executive Secretary
Minnesota Public Utilities Commission
121 Seventh Place East, Suite 350
St. Paul, MN 55101

VIA ELECTRONIC FILING

Re: In the Matter of the Petition of Minnesota Energy Resources Corporation for its Annual Review of Depreciation Rates for 2019
Docket No. G011/D-19-377

Reply Comments of Minnesota Energy Resources Corporation

Dear Mr. Wolf:

On May 31, 2019, Minnesota Energy Resources Corporation ("MERC" or the "Company") filed a Petition with the Minnesota Public Utilities Commission (the "Commission") requesting approval of its proposed depreciation rates effective January 1, 2019 and proposing modifications to its depreciation practices in compliance with the Commission's December 26, 2018 Findings of Fact, Conclusions, and Order in Docket No. G011/GR-17-563. In particular, MERC proposed updated remaining lives that reflect the passage of time as well as plant activity (additions and retirements) in its accounts. MERC also proposed to establish clear and objective criteria to apply in determining which of its existing buildings should be separated for purposes of depreciation and in what cases new buildings should be separately depreciated. The result of applying this criteria was to separate the Company's two largest buildings which account for 52 percent of the total book costs within Account 390, Structures and Improvements.

On August 9, 2019, the Minnesota Department of Commerce, Division of Energy Resources (the "Department") and the Minnesota Office of the Attorney General, Residential Utilities and Antitrust Division ("OAG") filed comments on the Company's Petition and proposal.

In its Comments, the Department concludes that MERC's proposed depreciation parameters and rates for all accounts other than Account 390 are reasonable.[1] The Department concludes that the Company's proposal reasonably complies with the requirement of the Commission's December 26, 2018, Order in Docket No. G011/GR-17-563, to propose a set of depreciation practices for the separate depreciation of large assets.[2] However, with respect to Account 390, the Department recommends that the Commission modify MERC's proposal and require the Company to depreciate the Rochester, Rosemount, Cloquet, and Albert Lea Service Centers individually and depreciate the other 18 buildings in Account 390 as members of the minor group.[3] The Department concludes MERC's proposed threshold to determine whether to individually depreciate buildings or not is unnecessary. Additionally, the Department requests that MERC provide additional information regarding the probable retirement year for the Cloquet Service Center in Reply Comments.

[1] Department Comments at 3.
[2] Department Comments at 2.
[3] Department Comments at 9.

In its Comments, the OAG recommends that the Commission take the following actions with respect to MERC's petition:

1. Require the Company to look at other existing large transmission or distribution assets, as well as any future large or unique assets to determine if the separate depreciation methodology would apply.

2. Require the Company to use a shorter remaining life for the major grouping in FERC Account 390 – Structures and Improvements, such as the curve used for the minor grouping of 45-R2.

3. Reject the Company's proposed rule for depreciating buildings individually, and require the Company to identify new or existing buildings that exceed a total book value of $1,000,000 in its future depreciation filings.

MERC thanks the Department and OAG for their review and comments and submits these Reply Comments in response to the recommendations and requests for additional information of the Department and OAG.

Initially, MERC notes that the OAG emphasizes the significance of theoretical depreciation reserves in its comments to support its recommendations.[4] However, because MERC employs a remaining life (as opposed to whole life) technique for its depreciation studies, the theoretical depreciation balance does not provide a meaningful data point as a required reserve amortization or reclassification. In particular, the theoretical depreciation balance is calculated assuming the depreciation parameters were in place since the inception of the account, while in practice, average service lives and net salvage can and do change over time as a result of regular depreciation studies adjusting for changes resulting from additions and retirements to plant or other changes.

Modifications to Depreciation Treatment of Existing & Future Assets

MERC's existing depreciation practices have previously been approved by the Department and Commission in the Company's annual depreciation dockets, and are consistent with the Federal Energy Regulatory Commission's Uniform System of Accounts and Generally Accepted Accounting Principles ("GAAP"). Nevertheless, MERC submitted a proposal to separately depreciate the Company's two newly constructed buildings that represent significant investments, consistent with the Commission's December 26, 2018, Findings of Fact, Conclusions, and Order in Docket No. G011/GR-17-563, which required:

> In either its next rate case or its next depreciation filing, whichever comes first, MERC shall propose a set of depreciation practices and adjustments for the separate depreciation of large assets, like office buildings or to provide explanation why no such modification from the Company's depreciation practices is warranted or appropriate.

[4] See OAG Comments at 5, 7 ("The Company's proposal has the potential to harm ratepayers because it creates a discrepancy between the theoretical reserve and the actual reserve collected from ratepayers.").

1. Criteria for Individually Depreciating Buildings

In the Company's May 31, 2019 Petition, MERC proposed to establish clear and objective criteria to apply in determining which of its existing buildings could be separated for purposes of depreciation and in what cases new buildings could be separately depreciated. The application of an objective standard for the evaluation of future additions is preferred in order to ensure consistency in the treatment of assets from the outset and to avoid potential disputes regarding the appropriate treatment of such assets for depreciation purposes. The result of applying MERC's proposed criteria is to separate the Company's two largest buildings, the Rochester and Rosemount Service Centers, which account for 52 percent of the total book costs within Account 390, Structures and Improvements.

The Department and OAG both advocate that the Company's proposed criteria be rejected in favor of alternate criteria to determine whether assets should be separately depreciated in the future.

- The Department states that building additions are infrequent and that evaluating them on a case-by-case basis will not be unduly burdensome. As a result, the Department asserts that MERC's proposed threshold is unnecessary. The Department also states that building cost is only one characteristic that should be considered in deciding whether a building should be depreciated individually. In particular, the Department argues "gross plant value is only one of many characteristics of a building, and adherence to a rule that ignores all other potential differentiating characteristics may in the future result in the inappropriate inclusion of a building with unique life and operational characteristics in the Minor buildings group."[5]

- The OAG also objects to the Company's proposed materiality threshold, stating that a monetary threshold should not be used to determine whether a building is depreciated individually. The OAG asserts that the determination should "not be based solely on the monetary relation to other existing assets, but rather should consider the asset itself, its value, and its characteristics."[6] The OAG recommends the Company should identify any new buildings in excess of $1,000,000 as well as improvements to existing buildings that result in the building's book value exceeding $1,000,000 so they can be reviewed for inclusion in the major grouping.

MERC believes its proposal as set forth in its May 31, 2019 Petition, to separate the Rochester and Rosemount buildings and to separate new buildings only when they are newly acquired or constructed and will constitute at least one percent of the Company's total depreciable net plant continues to be reasonable. This objective standard separates out individual buildings based upon a reasonable materiality standard that reflects changes over time; it is therefore preferable to both a fixed dollar threshold and a subjective determination based upon an asset's "characteristics."

Should the Commission adopt the OAG's recommendation of a $1,000,000 threshold for individually depreciating buildings, further refinements must be incorporated to recognize the impacts of inflation and to exclude the impacts of replacements that will occur periodically

[5] Department Comments at 7.
[6] OAG Comments at 6.

throughout a building's useful life. In particular, the following modifications should be applied to ensure the threshold remains reasonable.

1) The threshold should be adjusted annually to recognize the impact of year-over-year increases in the cost of construction. The Handy-Whitman Index of Public Utility Construction Costs is published annually, is widely used by utilities, and can be applied to inflate the threshold in future years. MERC would propose to use the North Central Region Gas Utility Construction January 2019 Structures and Improvements Index of 585 as the baseline index for this purpose.

2) The threshold should be applied at the time of acquisition or construction based upon the original cost of the building.

    a. Improvements may be made to existing buildings that result in the building's book value exceeding the threshold where those improvements are ongoing replacements expected to occur throughout the building's life such as replacements of roofs, HVAC equipment, etc. Such routine improvements do not extend the life of the building per se. Rather, such routine improvements are necessary repairs to keep the building in normal operation and should not cause a building to be reclassified from group depreciation to separate depreciation.

    b. In contrast, improvements resulting from an increase in the overall building footprint due to a building addition may be appropriate for consideration.

Application of a $1,000,000 threshold as recommended by the OAG would result in the separation of the Cloquet and Albert Lea Service Centers in addition to the Rochester and Rosemount buildings. There are additional impacts of making a change from group depreciation to separate depreciation that should be fully and appropriately addressed by the Commission should it accept the Department's and/or OAG's recommendations. In particular:

1) Reasonable and appropriate depreciation parameters should be set for the assets in the major and minor groupings of Account 390, and

2) MERC should be provided an opportunity to recover the resulting increase in annual depreciation expense through deferred accounting.

MERC addresses the impacts of modifying the current depreciation treatment and the appropriate resulting depreciation parameters and annual depreciation expense impacts below.

a. *Depreciation Parameters for Account 390 Major Grouping*

First, the depreciation parameters to be applied to the separated Service Centers must be reasonable and appropriate in consideration of the characteristics of these buildings. As the Department appropriately recognizes in its Comments, "[i]n order to depreciate the Rosemount, Rochester, Albert Lea and Cloquet Service Centers individually, lives, salvage rates, and beginning depreciation reserves must be determined for all [four] buildings."[7]

[7] Department Comments at 10.

In response to OAG Information Request No. 11, MERC conducted all of the analysis necessary to begin depreciating the Rochester, Rosemount, Cloquet, and Albert Lea Service Centers individually while depreciating the remaining 18 buildings as a group.[8] Table 1 below summarizes the results of that analysis for Rochester, Rosemount, Cloquet, and Albert Lea:

Table 1: Major Grouping Parameters

Building	Proposed Probable Retirement Year	Life Span (Years)	Remaining Life (Years)
Rochester	2063	55	41.5
Rosemount	2072	55	50.1
Cloquet	2035	55	16.0
Albert Lea	2072	55	50.1

Based on its review of MERC's analysis, the Department concludes the process used in MERC's response to OAG Information Request No. 11 is generally reasonable. However, with respect to the Cloquet Service Center, the Department notes that the proposed probable retirement year for Cloquet, 2035, reflects Cloquet's initial purchase year of 1980 and proposed 55 year life span. Further, the Department notes that, in its response to OAG Information Request No. 11, MERC stated that the use of a life span coupled with a truncated survivor curve does not appropriately reflect the building addition that was added to Cloquet in 1992 and produces an unreasonably short remaining life.[9] The Department recognizes the 1992 building addition at Cloquet likely extended its useful life and requests that MERC explain in reply comments why it cannot propose a probable retirement year that reflects those investments.[10]

MERC responds that while the 16 year remaining life calculated in response to OAG Information Request No. 11 may need to be adjusted in a future depreciation filing, MERC does not believe it can reasonably predict with certainty an alternate probable retirement date for this facility at this time. If the Commission requires Cloquet to be separately depreciated from the minor grouping, retaining the probable 2035 retirement year as reflected in MERC's response to OAG Information Request No. 11 at this time would be reasonable. The depreciable life of this building as well as other buildings can be adjusted as necessary through the Company's regular depreciation filings, as better information regarding probable retirement becomes available. While the Company has possible bookends based on the 1980 initial investment and 1992 expansion to the Cloquet Service Center, simply adding an additional 12 years to the remaining life could result in a remaining life that is too long.

As discussed in MERC's May 31, 2019 filing and responses to Department Information Request No. 3,[11] Department Information Request No. 4,[12] and OAG Information Request No. 10,[13] a building is comprised of multiple assets that are expected to experience interim retirements

[8] *See* MERC Response to OAG Information Request No. 11 (Included as Attachment 3 to the Department's Comments).
[9] Department Comments at 10.
[10] Department Comments at 10.
[11] Included as Attachment 4 to the Department's Comments.
[12] Attachment A to these Reply Comments.
[13] Attachment B to these Reply Comments.

throughout the overall building's life span—roofs, HVAC equipment, etc. Operational, functional, or structural considerations could all impact the timing of retirement for the Cloquet Service Center, as with any building. Therefore, MERC proposes to apply the probable retirement as reflected in the Company's Response to OAG Information Request No. 11, subject to further review and adjustment in future depreciation filings.

Including the Cloquet and Albert Lea Service Centers in the major group to be separately depreciated, MERC determined the proposed 55-year life span coupled with a 75-R2.5 interim survivor curve is most appropriate for each of the buildings based on statistical modeling, prior experience, industry practice, and informed judgment. The Department agreed that MERC's proposed 55-year life span coupled with a 75-R2.5 interim survivor curve, negative 10 percent salvage rate, and allocation method for the depreciation reserves is reasonable.[14]

In contrast, the OAG argues the Company selected an inappropriate interim survivor curve to determine the depreciation rate for the major grouping.[15] In particular, the OAG asserts that the proposed 75-R2.5 survivor curve is "not supported by the analysis provided by the Company and could result in an under-collection of depreciation reserve from ratepayers while the assets are in-service."[16] The OAG proposes that the Commission require MERC to use a shorter remaining life "such as the curve used for the minor grouping of 45-R2."[17] Alternatively, the OAG proposes that the Commission require the Company to use the same survivor curve of 55-R3 that was used for the major grouping in its most recent depreciation filing.[18] The OAG's proposal to arbitrarily apply the survivor curve that was calculated for an entirely different group of assets to the Rochester, Rosemount, Cloquet, and Albert Lea buildings is both unsupported and unreasonable.

First, the proposed 55 year life span and 75-R2.5 interim survivor curve are appropriately supported by consideration of MERC's experience, industry practice, and informed judgment with respect to the specific assets being evaluated.[19]

- MERC's proposed methodology includes two components to model depreciation expense and rate calculations—a life span and an interim retirement curve. The life span models retirements assuming the remaining assets at a location will be retired simultaneously at a specific date or at the end of a period of time. The end of life is when the structure is economically in need of replacement due to functionality, condition, etc.[20]

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[14] Department Comments at 11.
[15] OAG Comments at 3-4.
[16] OAG Comments at 1.
[17] OAG Comments at 5. Notably, this does not take into consideration the removal of the Cloquet and Albert Lea Service Centers from the minor grouping, as reflected in the Company's analysis provided in response to OAG Information Request No. 11.
[18] OAG Comments at 6.
[19] *See* OAG Comments at 5 ("The selection process should take into consideration recent Company behavior, industry practices, and informed judgment.").
[20] See MERC's Response to Department Information Request No. 4, included as Attachment A to these Reply Comments.

The Company employed an estimated end of life of 55 years for this purpose based on the Company's historic experience.[21]

- The Company used an interim survivor curve component to model retirements knowing that certain building assets (i.e., doors, roofs, HVAC equipment, etc.) will experience replacement prior to the retirement of the overall building. Based on an expected dispersion pattern of assets within the group while the assets are in service, the Company employed a 75-R2.5 survivor curve to represent the physical life characteristics for the 55 years until the rehabilitation or closure of the building is expected.

The OAG argues that MERC's analysis does not support a survivor curve that is "different from the survivor curve used in the last depreciation filing for the major grouping of FERC Account 390 – Structures and Improvements."[22] However, the 55-R3 survivor curve that had been approved in MERC's prior two depreciation studies for the major grouping of Account 390 was based solely on the Rochester Service Center. Because the Rochester Service Center was the only building in the grouping, had a recent vintage, and limited historical retirement activity, more limited data was available for the establishment of that survivor curve. MERC's proposed 55 year life span coupled with a 75-R2.5 interim survivor curve more accurately reflects the life characteristics of the larger service centers. The life characteristics of a large service center include the physical life of the components of the building while in service from year to year and the end of life when the structure is economically in need for replacement due to functionality or condition. The 75-R2.5 survivor curve represents the physical life characteristics for the 55 years until rehabilitation or closure of the building is expected.

Second, the OAG claims that the 55-R3 survivor curve follows a shorter remaining life than MERC's proposed 75-R2.5 truncated survivor curve at 55 years. This is incorrect, reflecting the OAG's general misunderstanding of depreciation parameters.

Table 2 below compares the attributes for the Rochester and Rosemount Service Centers which the Company proposed to depreciate individually. As reflected in the table, the vintage year remaining life presented for the 75-R2.5 truncated survivor curve with a life span of 55 years is shorter than those for the same vintage year for the 55-R3 survivor curve and thereby results in increased depreciation expense, contrary to the OAG's claim.

[21] See MERC's Response to Department Information Request No. 3, included as Attachment 4 to the Department's Comments.
[22] OAG Comments at 4.

Table 2: Remaining Life Comparison

Rochester Service Center

Year [1]	75-R2.5 Remaining Life [2]	55-R3 Remaining Life [3]
2008	41.53	44.82
2012	42.04	48.65
2014	42.27	50.59

Rosemount Service Center

Year [1]	75-R2.5 Remaining Life [2]	55-R3 Remaining Life [3]
2017	50.12	53.52

Source

(1) Column 1 of Calculated Remaining Life Depreciation Accrual (supporting schedule from Attachment 3 of the Petition)

(2) Column 6 of Calculated Remaining Life Depreciation Accrual using a 55 year life span (supporting schedule from Attachment 3 of the Petition)

(3) Iowa Survivor Mortality Curves and Remaining Lives from PowerPlan Reserve Ratio Table

In further response to the OAG's assertion that the 75-R2.5 survivor curve is unsupported, MERC's consultant, Gannett Fleming, concluded as part of its analysis from OAG Information Request No. 11 that historical activity including all four buildings does support the selected 75-R2.5 interim survivor curve.

Finally, the OAG argues the Company should use an even shorter remaining life from what was approved in Docket No. G011/D-17-442 for the major grouping, such as the 45-R2 survivor curve used for the minor grouping. The OAG's proposal to use a 45-R2 survivor curve would arbitrarily shorten the life of the major grouping, causing even higher depreciation rates and resulting depreciation expense. Despite advocating that selection of an appropriate survivor curve should take into consideration "recent Company behavior, industry practices, and informed judgment,"[23] the OAG provides no support for its recommendation of applying the minor grouping's survivor curve for the major grouping.

Because the OAG's suggestion is unreasonable and unsupported by statistical analysis, industry practice, informed judgment, or any other relevant consideration, it should be rejected. Neither the 45-R2, the revised 45-S0 from OAG Information Request No. 11, nor similar survivor curve determined to be appropriate for the minor grouping of Account 390 is reasonable or appropriate to be applied to the major grouping. Rather, MERC's proposed 55 year life span coupled with a 75-R2.5 interim survivor curve is most appropriate for the separately depreciated buildings.

[23] OAG Comments at 5.

b. Depreciation Parameters for Account 390 Minor Grouping

Any change to the Company's current depreciation practices to remove existing assets from the Account 390 minor grouping will impact that grouping's depreciation parameters as well as the Company's annual depreciation expense.

Specifically, the exclusion of the Cloquet and Albert Lea Service Centers from the minor grouping as recommended by the Department and OAG results in changes to the vintage surviving plant used in depreciation study analytics for the remaining minor grouping assets. As a result, the 45-R2 survivor curve for the minor grouping is no longer statistically supported. As discussed in MERC's response to OAG Information Request No. 11, a 45-S0 survivor curve would be more statistically appropriate for the remaining assets in that group.

The resulting change to the minor grouping's survivor curve has further implications. The use of a 45-S0 survivor curve results in a revised calculated theoretical depreciation reserve and resulting ratio. As explained in response to OAG Information Request No. 11, the calculated theoretical reserve would increase from $3,790,607 to $3,976,776 and a corresponding change would have to be made in the ratio from 68% to 65%. The change in the ratio further impacts the calculated remaining life and annual depreciation rate for each building in the major grouping as well as the minor grouping.

c. *Impacts to Annual Depreciation Expense*

Finally, the modifications to existing depreciation practices will impact the Company's annual depreciation expense. Acceptance of the proposal to separate Rochester, Rosemount, Cloquet and Albert Lea result in an increase to annual depreciation expense for 2019 of approximately $64,000.[24] Because this financial impact will occur outside of a general rate case proceeding, the Company will not be provided an opportunity to recover the resulting additional annual expense. As a result, MERC requests authorization for deferred accounting treatment to track the increase in annual depreciation expense for recovery in its next rate case.

> Deferred accounting is a regulatory tool used primarily to hold utilities harmless when they incur out-of-test-year expenses related to utility operations for which ratepayers have incurred costs or received benefits that, because they are unforeseen, unusual, and large enough to have a significant impact on the utility's financial condition, should be eligible for rate recovery in the next rate case. Expenses for which deferral is requested must also be subject to review for reasonableness and prudence.[25]

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[24] As discussed in MERC's Response to OAG Information Request No. 11 (included as Attachment 3 to the Department's Comments), separation of the Rochester and Rosemount buildings would result in an increase in annual depreciation expense of approximately $32,000. If the Commission's actions determine it is appropriate to individually depreciate additional buildings as proposed by the Department and the OAG, depreciation expense is anticipated to increase an additional $32,000 using the depreciation parameters of 75-R2.5 for major building and 45-S0 for minor buildings for a total of $64,000 annually.

[25] *In the Matter of a Petition for Approval of Deferred Accounting Treatment of Costs Related to the 2016*

The increase in annual depreciation expense costs are (1) related to MERC's operations for which ratepayers have incurred costs or received benefits; (2) significant in amount, (3) unusual and extraordinary, and (4) will be subject to review for reasonableness and prudence in a future rate proceeding.

First, the assets in Account 390, Structures and Improvements, are necessary and related to MERC's operations and the provision of natural gas service to customers. The Department and OAG have advocated that separation of the Rochester, Rosemount, Cloquet, and Albert Lea buildings for depreciation purposes will benefit ratepayers by more closely tracking the anticipated retirement of such assets to avoid the impact of undepreciated plant balance at the end of the building's life.

Second, while the annual impact to depreciation expense is only $64,000, absent authorization for deferral, MERC will be denied the ability to recovery that amount each year until it files a subsequent rate case. Because the proposed modifications to the Company's existing depreciation practices are occurring outside of a rate case, MERC should be allowed an opportunity to recovery the resulting increase in annual expense. The intent of the proposed changes to depreciation practices is to ensure the recovery of depreciation expense most accurately aligns with the useful lives of the assets. To order such changes without providing the company an opportunity to recover the actual increase in expense would be unreasonable.

Third, to make such changes to existing depreciation practices outside a rate case (as well as outside of a full depreciation study) is unusual. While the Company agreed in Docket No. G011/GR-17-563 to evaluate the continued reasonableness of its depreciation practices for larger buildings, the separate depreciation of four buildings is a significant change from current practice.

Finally, MERC agrees that its actual depreciation expense will be subject to review for prudence and reasonableness in a future rate proceeding.

Because the increase to annual depreciation expense will occur outside of a general rate case proceeding, the Company will not be provided an opportunity to recover the additional annual expense until if files a subsequent rate case. As a result, MERC requests authorization for deferred accounting treatment to track the increase in annual depreciation expense for recovery in its next rate case.

Evaluation of Other Assets

In its Comments, the OAG also proposes that MERC evaluate other existing large transmission or distribution assets as well as any future large or unique assets to determine whether separate depreciation methodology should be applied. MERC responds that the Company reviews its assets as part of this annual depreciation update process and has already concluded that group depreciation continues to be the most appropriate method for depreciating transmission and distribution assets. No additional review is necessary.

In the context of utility accounting there are two independent justifications for the application of group accounting for utility assets: (1) with respect to certain fixed assets such as utility poles

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Storm Response and Recovery, Docket No. E015/M-16-648, Order Denying Petition for Deferred Accounting Treatment at 2 (Jan. 10, 2017).

and other components of the transmission and distribution system, the components are too numerous to practically track on an individual basis given the small relative value of each individual asset; and (2) with respect to larger assets like buildings that are comprised of numerous components and parts, it is impractical to separately track all components, especially when the components are typically inseparable from the building (e.g., a roof or HVAC system).

As explained in PwC interpretive guidance regarding utility asset retirement, and depreciation:

> Two methods of depreciating multiple-asset accounts are employed: the group method and the composite method. The term "group" refers to a collection of assets that are similar in nature. "Composite" refers to a collection of assets that are dissimilar in nature.
>
> …
>
> Utilities often apply the mass-asset convention of accounting (also known as the "group" method) to certain fixed assets such as utility poles and other components of their transmission and distribution systems which are too numerous to practically track on an individual basis given the small relative value of each individual asset. Similarly, many utility companies utilize the composite convention of accounting for component parts of larger assets such as electric generating stations which also contain numerous components and parts which are impractical to separately track.[26]

As MERC is a gas distribution company, its distribution and transmission property includes many dispersed but interrelated assets. These assets, numbering in the tens of thousands, are recorded at a vintage year, size, material type, and municipal tax reporting level. As such, these assets represent a large number of similar assets for which additions and retirements occur continually and systematically over time and the life of any one unit is not dependent on the life of any of the other units. As a result, the assets are widely dispersed and have a variety of costs which are not conducive to individual depreciation.

Unlike an electric utility, which may own generating stations or other similar large facilities, MERC does not own any assets outside of Account 390 that would support separate accounting treatment. Group depreciation continues to be the most appropriate method for depreciating MERC's natural gas transmission and distribution assets.

Conclusion

In conclusion, separately depreciating major service center buildings is reasonable only if appropriate depreciation parameters as outlined above are applied to those assets and to the remaining minor grouping of Account 390. Further, because such changes to existing depreciation practices will result in an increase in annual depreciation expense outside of a general rate case proceeding, the Company will not be provided an opportunity to recover the

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[26] PriceWaterhouseCoopers, Questions and Answers, Interpretations for the Utility Industry, Accounting for Property, Plant and Equipment, Asset Retirement Obligations and Depreciation (available at https://www.pwc.com/gx/en/energy-utilities-mining/pdf/ppe.pdf).

additional annual expense until it files a subsequent rate case. As a result, MERC requests authorization for deferred accounting treatment to track the increase in annual depreciation expense for recovery in its next rate case.

The Commission should also establish appropriate parameters for the evaluation of whether assets should be separated for depreciation purposes in the future. As discussed above, MERC continues to recommend that new buildings be separated only when they are newly acquired or constructed and will constitute at least one percent of the Company's total depreciable net plant. If the Commission accepts the OAG's alternative recommendation of a $1,000,000 threshold for individually depreciating buildings, further refinements must be incorporated to recognize the impacts of inflation and to exclude the impacts of replacements that will occur periodically throughout a building's useful life.

Please contact me at (414) 221-2374 if you have any questions regarding the information in this filing. Thank you for your attention to this matter.

Sincerely,

/s/ Mary L. Wolter
Mary L. Wolter
Director – Gas Regulatory Planning & Policy

Enclosures
cc: Service List

Minnesota Department of Commerce
Division of Energy Resources
Information Request

Docket Number:	G011/D-19-377	☐Nonpublic	☒Public
Requested From:	Minnesota Energy Resources Corp.	Date of Request:	June 17, 2019
Type of Inquiry:	Financial	Response Due:	June 27, 2019

Requested by:	Craig Addonizio
Email Address(es):	craig.addonizio@state.mn.us
Phone Number(s):	651-539-1818

Request Number: 4

Topic:	Account 390 Major Grouping Interim Retirement Curve
Reference(s):	Petition, Attachment 3, page 7

Request:

a. The Company's Petition states that proposed interim survivor curve of 75-R2.5 was "determined through historical analysis and informed judgement." Please provide all historical analysis used to support the selection of this curve.

b. Does the selection of the 75-R2.5 survivor curve imply that the components of these buildings are expected to have an average service life of 75 years, and are therefore expected to outlive, on average, the building itself (which is assumed to have a 55-year life)? If so, please explain why this is not contradictory.

Response:

a. The historical analysis referenced in that statement was represented in the Depreciation Study presented in Docket No. G-011/D-17-442. In the case of the major grouping, there were no recorded retirements in the first eight years of activity for the Rochester Service Center and the Rosemount Service Center had not been placed in service. The major grouping in this Docket is now introducing the use of a life span coupled with an interim survivor curve. Based on the above, a 75-R2.5 interim survivor curve was selected to depict estimated future retirement activity with a planned end of life. The primary factor for the 75-R2.5 interim survivor curve is informed judgment. The informed judgment includes understanding the type facility, plans for

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To be completed by responder

Response Date: June 27, 2019
Response by: John Spanos – Gannett Fleming Valuation and Rate Consultants, LLC (contact information via MERC – Tina Wuyts)
Email Address: tina.wuyts@wecenergygroup.com
Phone Number: 920-433-4951

Minnesota Department of Commerce
Division of Energy Resources
Information Request

Docket Number:	G011/D-19-377	☐Nonpublic	☒Public
Requested From:	Minnesota Energy Resources Corp.	Date of Request:	June 17, 2019
Type of Inquiry:	Financial	Response Due:	June 27, 2019

Requested by:	Craig Addonizio
Email Address(es):	craig.addonizio@state.mn.us
Phone Number(s):	651-539-1818

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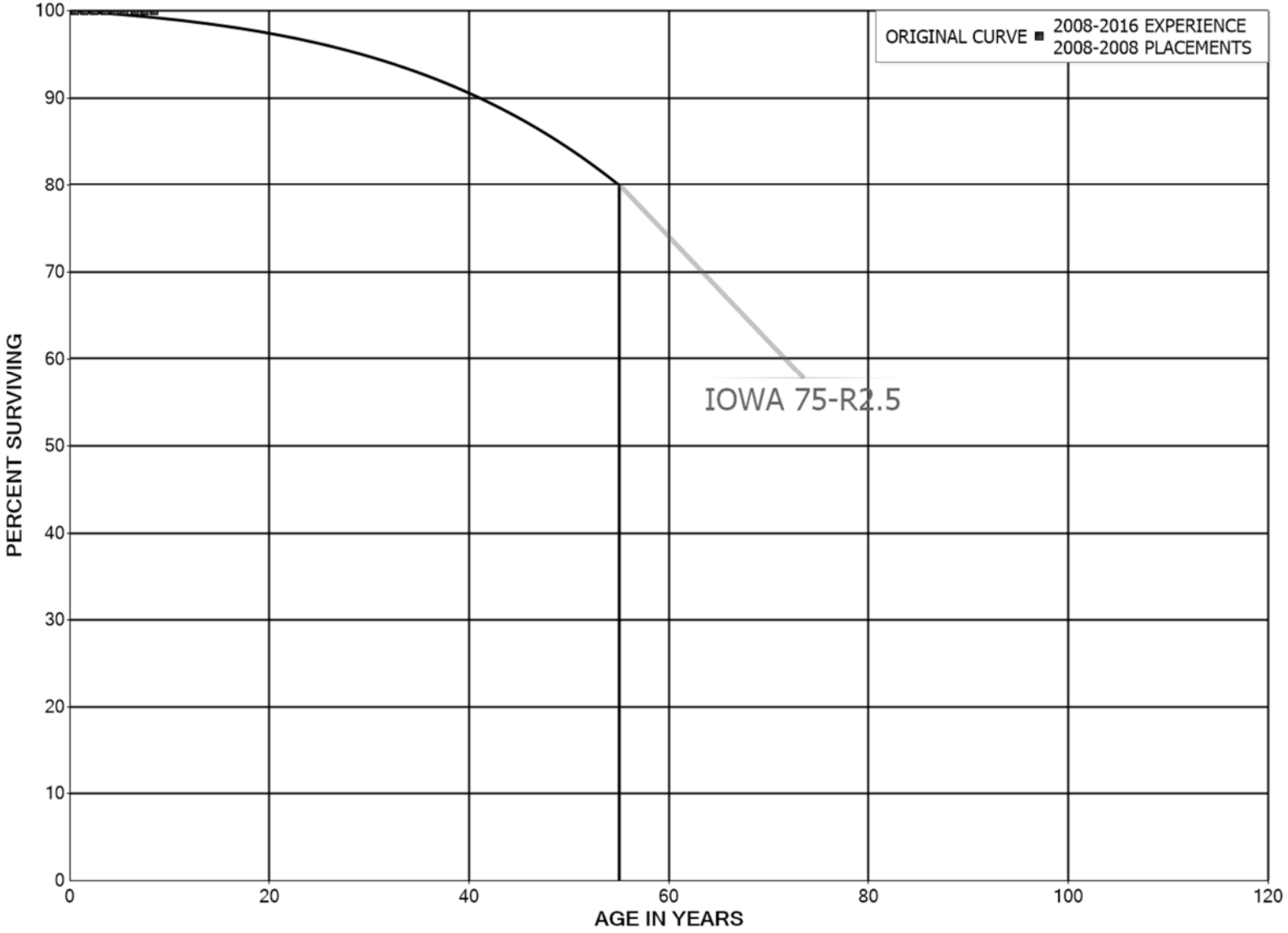
outlook of the facilities and estimates of others in the industry for similar structures. As noted in Attachment 3 of MERC's 2019 Annual Review of Depreciation Rates, the 75-R2.5 represents an interim survivor curve used in conjunction with a 55 year life span. This is shown in the attached file.

b. The life characteristic of a large service center has two components. One is the physical life of the components of the building while in service from year to year. The other component is the end of life when the structure is economically in need of replacement due to functionality, condition, etc. The 75-R2.5 survivor curve represents the physical life characteristics for the 55 years until the rehabilitation or closure of the building is expected. Therefore, the 75-R2.5 survivor curve does not imply that the components of the building will outlive the building itself. The two life components are not directly related.

To be completed by responder

Response Date: June 27, 2019
Response by: John Spanos – Gannett Fleming Valuation and Rate Consultants, LLC (contact information via MERC – Tina Wuyts)
Email Address: tina.wuyts@wecenergygroup.com
Phone Number: 920-433-4951

MINNESOTA ENERGY RESOURCES CORPORATION
ACCOUNT 390.00 STRUCTURES AND IMPROVEMENTS - MAJOR
ORIGINAL AND SMOOTH SURVIVOR CURVES



MINNESOTA ENERGY RESOURCES CORPORATION

ACCOUNT 390.00 STRUCTURES AND IMPROVEMENTS - MAJOR

ORIGINAL LIFE TABLE

PLACEMENT BAND 2008-2008 EXPERIENCE BAND 2008-2016

AGE AT BEGIN OF INTERVAL	EXPOSURES AT BEGINNING OF AGE INTERVAL	RETIREMENTS DURING AGE INTERVAL	RETMT RATIO	SURV RATIO	PCT SURV BEGIN OF INTERVAL
0.0	3,224,389		0.0000	1.0000	100.00
0.5	3,224,389		0.0000	1.0000	100.00
1.5	3,224,389		0.0000	1.0000	100.00
2.5	3,224,389		0.0000	1.0000	100.00
3.5	3,224,389		0.0000	1.0000	100.00
4.5	3,224,389		0.0000	1.0000	100.00
5.5	3,224,389		0.0000	1.0000	100.00
6.5	3,224,389		0.0000	1.0000	100.00
7.5	3,224,389		0.0000	1.0000	100.00
8.5					100.00

OAG No. 010

State Of Minnesota
Office Of The Attorney General
Utility Information Request

In the Matter of the Petition of Minnesota Energy Resources Corporation for its Annual Review of Depreciation Rates for 2019		**MPUC Docket No.**	G-011/D-19-377

Requested from: MERC

By:	Shoua Lee	**Date of Request:**	July 11, 2019
Telephone:	(651) 757-1417	**Due Date:**	July 23, 2019

Reference: Account 390 Major - Calculated Remaining Life Depreciation Accrual spreadsheet

Provide documentation that supports the Company's use of a 50 year remaining life for the Rosemount Service Center, and a 41 year remaining life for the Rochester Service Center.

Explain why the remaining life of each building does not match the 55 year life span the Company is using.

MERC Response:

The remaining life of each location recognizes the passage of time from when each building was placed in service. As discussed in Attachment 3 of the Petition, MERC introduced a life span coupled with an interim retirement curve to address separately depreciating the Rochester and Rosemount buildings. While the life span uses the building's estimated end of life of 55 years, the interim retirement curve addresses asset retirements that are expected to occur prior to each building's end of life. The surviving vintage plant for each building uses a corresponding remaining life data point from the truncated interim retirement curve to calculate a remaining life. OAG Information Request No. 4 provides additional details for the calculation of a remaining life. As Rochester and Rosemount have different vintage year surviving plant, the calculated remaining life is different from one another.

Response by Greg Cieslewicz
Title Lead Analyst
Department Property Accounting
Telephone 920-433-1087

In the Matter of the Petition of Minnesota Energy Resources Corporation for its Annual Review of Depreciation Rates for 2019	Docket No. G011/D-19-377

CERTIFICATE OF SERVICE

I, Kristin M. Stastny, hereby certify that on the 28th day of August, 2019, on behalf of Minnesota Energy Resources Corporation (MERC), I electronically filed a true and correct copy of the enclosed Reply Comments on www.edockets.state.mn.us. Said documents were also served via U.S. mail and electronic service as designated on the attached service list.

Dated this 28th day of August, 2019.

/s/ Kristin M. Stastny
Kristin M. Stastny

First Name	Last Name	Email	Company Name	Address	Delivery Method	View Trade Secret	Service List Name
Michael	Ahern	ahern.michael@dorsey.com	Dorsey & Whitney, LLP	50 S 6th St Ste 1500 Minneapolis, MN 554021498	Electronic Service	No	OFF_SL_19-377_D-19-377
Generic Notice	Commerce Attorneys	commerce.attorneys@ag.state.mn.us	Office of the Attorney General-DOC	445 Minnesota Street Suite 1800 St. Paul, MN 55101	Electronic Service	Yes	OFF_SL_19-377_D-19-377
Sharon	Ferguson	sharon.ferguson@state.mn.us	Department of Commerce	85 7th Place E Ste 280 Saint Paul, MN 551012198	Electronic Service	No	OFF_SL_19-377_D-19-377
Daryll	Fuentes	dfuentes@usg.com	USG Corporation	550 W Adams St Chicago, IL 60661	Electronic Service	No	OFF_SL_19-377_D-19-377
Brian	Meloy	brian.meloy@stinson.com	STINSON LLP	50 S 6th St Ste 2600 Minneapolis, MN 55402	Electronic Service	No	OFF_SL_19-377_D-19-377
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Catherine	Phillips	catherine.phillips@we-energies.com	We Energies	231 West Michigan St Milwaukee, WI 53203	Electronic Service	No	OFF_SL_19-377_D-19-377
Generic Notice	Residential Utilities Division	residential.utilities@ag.state.mn.us	Office of the Attorney General-RUD	1400 BRM Tower 445 Minnesota St St. Paul, MN 551012131	Electronic Service	Yes	OFF_SL_19-377_D-19-377
Elizabeth	Schmiesing	eschmiesing@winthrop.com	Winthrop & Weinstine, P.A.	225 South Sixth Street Suite 3500 Minneapolis, MN 55402	Electronic Service	No	OFF_SL_19-377_D-19-377
Colleen	Sipiorski	Colleen.Sipiorski@wecenergygroup.com	Minnesota Energy Resources Corporation	700 North Adams St Green Bay, WI 54307	Electronic Service	No	OFF_SL_19-377_D-19-377

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Mary	Wolter	mary.wolter@wecenergygroup.com	Minnesota Energy Resources Corporation (HOLDING)	231 West Michigan St Milwaukee, WI 53203	Electronic Service	No	OFF_SL_19-377_D-19-377
Tina E	Wuyts	tina.wuyts@wecenergygroup.com	Minnesota Energy Resources Corporation	PO Box 19001 700 N Adams St Green Bay, WI 54307-9001	Electronic Service	No	OFF_SL_19-377_D-19-377