MINNESOTA
PUBLIC UTILITIES COMMISSION

# Staff Briefing Papers

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| Meeting Date | December 20, 2018 | Agenda Item * 11 |
| Company | Great Plains Natural Gas Co. (Great Plains), a Division of MDU Resources Group, Inc. | |
| Docket No. | **G-004/D-18-369** | |
| | **In the Matter of Great Plains Natural Gas Co.'s Petition for Approval of its 2018 Depreciation Certification** | |
| Issues | Should the Commission approve Great Plains Natural Gas Co.'s 2018 depreciation certification? | |



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| ✓ **Relevant Documents** | **Date** |
|---|---|
| Great Plains Natural Gas – Initial Filing | June 1, 2018 |
| Department of Commerce – Comments | August 16, 2018 |
| Great Plains Natural Gas – Reply Comments | October 4, 2018 |
| Great Plains Natural Gas – Supplemental Reply Comments | November 5, 2018 |
| Department of Commerce – Response Comments | November 13, 2018 |
| Great Plains Natural Gas – Reply Comments | December 3, 2018 |
| Department of Commerce – Supplemental Response Letter | December 10, 2018 |

## I. Statement of the Issues

Should the Commission approve Great Plains Natural Gas Co.'s 2018 depreciation certification?

## II. Background

On June 1, 2018, Great Plains Natural Gas Co. (Great Plains, GPNG of the Company), a Division of MDU Resources Group, Inc., petitioned for approval of a Depreciation Certificate pursuant to Minn. Stat. § 216B.11 and Minn. Rules, Parts 7825.0500 to 7825.0900. This submission is also required by the Minnesota Public Utilities Commission's (Commission) December 4, 2017 Order in Docket No. G-004/D-17-450 which required Great Plains' next annual depreciation filing to be submitted by June 1, 2018.

In its Petition, Great Plains stated that this Annual Depreciation Study updates its five-year study from Docket No. G-004/D-17-450 to reflect the plant-in-service and book depreciation reserve balances as of December 31, 2017. The update results in an increase of $2,942 over current depreciation expense, resulting in a proposed composite depreciation rate of 4.32 percent versus 4.31 percent in its five-year study.

Great Plains requested an effective date of January 1, 2018 for the proposed rates.

On August 16, 2018, the Minnesota Department of Commerce, Division of Energy Resources (Department) filed comments, noting that this 2018 Depreciation Study is the first update to Great Plains' most recent five-year depreciation study.[1] The Department's comments included five attachments detailing Great Plains' responses to the Department's information requests. However, the Department indicated it would need additional information in four areas before it could adequately evaluate and make a recommendation on the proposed depreciation rates in Great Plains 2018 Depreciation Study.

On October 4, 2018, Great Plains filed its response and provided additional information as well as a revised 2018 Technical Depreciation Update from its consultant Concentric Advisors.

On November 5, 2018, Great Plains provided supplemental reply comments indicating an additional $367 discrepancy in its proposed depreciation rate for Account 396.1 Power Operated Equipment – Trailers. In addition, Great Plains explained that Accounts 396.1 and 396.2 were analyzed, in the past, as one account. The new depreciation consultant Concentric Advisors has now separated these accounts.

On November 13, 2018, the Department submitted response comments summarizing its review and recommending approval of Great Plains' proposed depreciation rates as provided in its supplemental reply comments filed November 5, 2018.

On December 3, 2018, Great Plains submitted reply comments to the response comments of the Department, re-affirming its agreement with the Department's recommendation of

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[1] Docket No G-004/D-17-450 (2017 Depreciation Docket).

approval of the depreciation parameters and the resulting depreciation rates. Additionally, Great Plains agreed with the Department's recommendation to change its plant-in-service reporting basis in all future Jurisdictional Annual Reports to reflect Minnesota jurisdictional amounts for the gas plant-in-service accounts. However, the Company expressed concerns regarding the Department's request that Great Plains individually report depreciation data for regulatory utility operations buildings in Account No. 390 – General Structures and Improvements.

On December 10, 2018, the Department filed a letter requesting that the Commission direct Great Plains, in its next depreciation filing, to provide data on individual utility service buildings that are currently accounted for as group assets.

# III. Parties' Comments

## A. Great Plains Natural Gas Co. – Initial Petition

In Great Plains' initial filing, the Company states that the application of the proposed depreciation rates results in an increase of $2,942 from the current depreciation expense in Docket No. G004/D-17-450. The composite annual depreciation rate has increased from 4.31 percent to 4.32 percent.

## B. Department of Commerce - Comments

The Department reviewed GPNG's compliance with filing requirements and previous commission orders and stated that:

1. Great Plains is in compliance with the requirement that it use its most recently approved depreciation rates which were based on the straight line depreciation method approved in Docket No. G-004/D-17-450 to calculate depreciation expense in 2017.

2. Great Plains' 2018 annual Depreciation Study, when supplemented with Great Plains' response to DOC Information Request No. 14 (disclosure of additions, retirements, adjustments, and transfers of the plant-in-service and associated accumulated depreciation) meets all relevant filing requirements.

3. Great Plains proposed depreciation rates to be effective January 1, 2018 based on December 31, 2017 plant and reserve balances are reasonable.

The Department indicated it would need additional support and information in four areas before it could adequately evaluate and make a recommendation on the rates in Great Plains 2018 Depreciation Study. The Department requested GPNG's explanation regarding the following four Department observations:

1. *Vintage Group Basis* versus *Broad Group Basis* – although Great Plains indicated that "the depreciation rates in this update have been calculated using the same depreciation methods, procedures and techniques employed in the last GPNG depreciation study", the Department learned through discovery that Great Plains had changed the basis for its remaining life calculations from a "*Broad Group*" basis to a "*Vintage Group*" basis.

a) Significant Change in Rates for Accounts 396.1 and 396.2 – Power Operated Equipment. In this filing, the use of a single general account was discontinued and the assets were divided and analyzed in two separate sub-accounts: *396.1 Power Operated Equipment – Trailers* and 396.2 *Power Operated Equipment*. Both of the proposed depreciation rates – 2.20 percent for account 396.1 and 1.23 percent for account 396.2 are significantly different from the last single rate of negative 2.89 percent.

2. New Survivor Curves Used. In Great Plains prior study, there were no survivor curves assigned to five general plant accounts. Instead, the depreciation amortization rates were established using a predetermined life assigned to each plant category that did not take into account the accumulated depreciation position. In this study, GPNG has assigned survivor curves, but only to four of the five accounts (391.3 Computer & Electronic Equipment did not use the survivor curve). Great Plains did not clearly highlight and explain this changed approach in depreciation rate development.

3. Proposed Use of Prior Year Approved Rate. The Company continued to use the prior year's approved depreciation rate for distribution plant accounts 378.0, 381.0, and 383.0. The rate developed for these accounts reflected the planned PVC Replacement program, however GPNG did not provide an update on the status of this program.

## C. Great Plains Natural Gas Co. – Reply Comments

Great Plains provided additional information and explanation for each of the areas requested by the Department:

1. *Vintage Group Basis* versus *Broad Group Basis*. Great Plains and its consultant Concentric Advisors note that clarification regarding the remaining life calculations used in the current docket as compared to those used in prior dockets is required.

> *"It appears that the terminology related to the use of the Vintage Group approach to remaining life calculations used in response to Minnesota Department of Commerce Information Request No. 2, inadvertently implied that the Vintage Group Model (or <u>Procedure</u>) was used. For clarity, the depreciation calculations used in this docket were performed using the Straight-Line method, the Average Life Group (Broad Group) Procedure, and applied on a remaining life basis. This is unchanged from prior dockets. However, the refinement made in this docket related to the application of a remaining life basis on a Vintage Group approach."*

Additionally, Great Plains stated that it will commit to continue the use of the current approach in future technical updates and Concentric Advisors is now being used for depreciation updates by its other utility subsidiaries.

2. Significant Change in Rates for Accounts 396.1 and 396.2 – Power Operated Equipment. In the previous study these two accounts were combined into a single account – 396.0 Power Operated Equipment. For this update, Great Plains chose to keep the accounts separate as per the FERC accounts structure. Since the prior study the total amount of original costs increased from $961,851 to $1,253,367 for a total change of $291,517. At the same time, the total Book Depreciation Reserve decreased by $119,001 including retirements and salvage proceeds of $242,179. The impact of these changes was an increase in the total depreciation rate to 1.35% from negative 2.89% in the prior study.

3. New Survivor Curves Used. Per Great Plains' response:

   > *"The use of a square curve is, in fact, an amortization approach. However, prior depreciation studies have incorporated the use of amortization accounting (or square curves) on a Whole Life Basis, rather than on a Remaining Lives Basis. As such, there was no change in approach in the use of using square curves versus the previously approved amortization accounting approach."*

4. Proposed Use of Prior Year Approved Rate. Great Plains' responded that it is continuing its mains and services program which nearly 42% complete. The Company promised to continue to monitor the status of the PVC replacement program and will provide a more robust analysis in its next technical update.

5. Additionally, Great Plains' response included details on several discrepancies and corrections. As previously mentioned, in the transition of records to and between Concentric Advisors and the previous consultant, the assets in several accounts encountered errors in the original investment by vintage which have all been corrected.

### D. Great Plains Natural Gas Co. - Supplemental Reply Comments

Great Plains' supplemental reply comments contained a complete 2nd Revised Technical Update from Concentric Advisors. This update included a small correction for one additional discrepancy in Account 396.1 resulting in increased depreciation of $367. The Company summarized by stating that the total change in this revised depreciation study versus its June 1st study is a decrease in annual depreciation expense of $4,428.

### E. Department of Commerce - Response Comments

In its response comments, the Department points out that the depreciation rates in GPNG's final, corrected "2018 Second Revised Study" from November 5th, when applied to plant balances as of December 31, 2017, results in a total depreciation expense amount of $2,273,242 which is a $4,428 reduction when compared to the Company's initial petition proposal. Table 1[2] below is a summary of the 2018 Second Revised Study results aggregated by system function, and compared to the prior 2017 depreciation study.

**TABLE 1**

| Plant Group | Original Cost | 2017 Study Annual Accrual | | 2018 Second Revised Study Annual Accrual | |
|---|---|---|---|---|---|
| Transmission Plant | $ 2,555,239 | 1.75% | $ 44,717 | 1.24% | $ 31,558 |
| Distribution Plant | $ 43,806,947 | 4.57% | $ 2,001,978 | 4.55% | $ 1,991,946 |
| General Plant | $ 6,334,250 | 3.60% | $ 228,033 | 3.94% | $ 249,738 |
| **TOTAL** | $ 52,696,436 | 4.32% | $ 2,274,728 | 4.31% | $ 2,273,242 |

*As the Department notes, it is important to realize that these are composite summarized rates and are not the actual rates that are applied at an account level.*

1. *Vintage Group Basis* versus *Broad Group Basis*. The Department stated that the annual depreciation developed in prior studies was calculated by dividing the annual depreciation accrual amount by the original cost of plant balance. However, the numerator in this formula (i.e. the annual depreciation accrual amount) was developed differently – using the *average remaining life for the vintage age* in the instant study compared to prior studies which used a *weighted average remaining life of the group*.

The Department believes this petition is not simply an annual update but, rather, is a proposal for changes that are more appropriately requested, evaluated, and established in a five-year depreciation study. As indicated by Great Plains, the Company is committed to continue the use of the current approach in future updates and if further changes in method are proposed, would only be done in the scope of a new five-year study.

The Department recommends the Commission record this commitment by the Company in its order. In addition, the Department notes that one other Minnesota regulated utility is using the same technique that GPNG now uses in its depreciation study. Therefore, the Department believes this approach is acceptable in developing depreciation accruals and rates.

2. Significant Change in Rates for Accounts 396.1 and 396.2 – Power Operated Equipment. Great Plains explained that plant retirements in 2017 reduced the depreciation reserve for these accounts. The retirements and major plant additions not only changed the age-complement of the asset group, but the corresponding depreciation reserve position from over depreciated to a need for depreciation to be accrued. The Department believes this concern is resolved.

3. New Survivor Curves Used. Great Plains' stated that the designation of a square curve for the five plant accounts is not new, what has changed between studies is that the depreciation technique was changed from a whole life approach to a remaining life approach. The Department believes this issue has been reasonably resolved.

4. Proposed Use of Prior Year Approved Rate. Great Plains is in the midst of a 15 year PVC replacement program and this program is now 42% complete. The PVC program is affecting accounts 378.0 - *Measuring and Regulating Station Equipment General*, 381.0 –

[2] Source: GPNG Supplemental Reply Comments (November 5, 2018) Attachment A, p. 1-1.

*Meters & Meter Installations*, and 383.0 – *House Regulators*. GPNG has committed to monitoring this program's status and to providing the Department and the Commission a more robust analysis in its next technical update. The Department recommends that the Commission record the Company's commitment to provide this analysis in its Order.

5. New Other Items

a. Great Plains' Minnesota Jurisdictional Annual Report. In a limited review of the Company's Jurisdictional Annual Report (JAR)[3] for activity through December 31, 2017, the Department discovered that the cost amounts for GPNG's gas plant-in-service accounts only reflect the cost of facilities physically located in Minnesota rather than the correct jurisdictional cost share of facilities serving Minnesota customers. The Department recommends that the reporting basis should change in future JAR filings. In addition, the Department recommends that the Commission direct GPNG's beginning-of-year gas plant-in-service balance reported in its 2018 JAR (to be filed in May, 2019) should be the jurisdictional amount, footnoted to explain the reason the balance differs from the 2017 year-end balances report.

b. Buildings used for Regulated Utilities Operation. The Department asks that the Commission direct the Company to provide, in its next filing, a schedule listing all buildings used for regulated utility operations, including cost amounts, individual or allocated depreciation reserve amounts, the depreciation rate and method applied to such asset, the placed-in-service dates, building address/location and operational purpose, and the identity of the FERC account in which the building is booked.

c. Schedules required by Minnesota Rule 7825.0700. Great Plains has committed to file, in future depreciation initial filings, schedules showing additions, retirements, adjustments, and transfer activity of the plant-in-service and their respective depreciation reserve accounts.

Overall, the Department concludes that Great Plains used the Commission-approved depreciation rates to calculate depreciation expense in 2017 and recommends that the Commission approve the Company's proposed 2018 Second Revised Depreciation Study, filed November 5, 2018.

## F. Great Plains Natural Gas Co. – Reply to Response Comments

Great Plains filed a reply to the Department's response comments on December 3, 2018, agreeing with the Department's recommendation for the Commission to approve the depreciation parameters and rates.

The Company agreed with the Department's recommended change to GP's future Jurisdictional Annual Reports to more accurately report the Minnesota jurisdictional amounts through changing its gas plant-in-service reporting basis. GP will also include footnotes to explain the reasons for differences in the 2017 year end balances in Docket No. E,G-999/PR-18-04 and the beginning-of-year balances reported in the 2018 JAR to be filed in May, 2019.

[3] Docket No. E,G-999/PR-18-04

However, Great Plains did express concerns regarding the Department's recommendation that it report regulatory utility operations buildings individually in future depreciation filings. The Company points out that, currently, these buildings are depreciated in Account 390 – General Structures and Improvements using a group asset method and a single average remaining life depreciation rate. While Great Plains does have records of the original cost for these assets, the accumulated reserve is not maintained on an individual basis. Since, on disposition, the retirement cost of an individual building is closed to the accumulated reserve account, allocation of the remaining reserve balance to individual buildings would be complicated.

### G. Department of Commerce – Supplemental Response Letter

The Department filed a letter expressing its desire to better understand how Minnesota regulated utilities account for buildings used in utility functions, particularly the treatment of additions and retirements. The Department repeated its request that Great Plains, in its next depreciation filing, provide a schedule listing "all buildings used for regulated utility operations, including their cost amounts, their individual or allocated depreciation reserve amounts, the depreciation rate and method applied to such assets, the placed-in-service dates, building address/location and its operation purpose, and finally to identify the account in which the listed building asset is booked".

The Department states that the requested information is important in the context of assessing the appropriateness of applying group accounting depreciation methods to utility service buildings that may vary in size and function.

## IV. Staff Comments

All parties agree in recommending that the Commission approve Great Plains' annual depreciation study and its parameters and rates. Additionally, Great Plains agrees with the Department's recommendations on correcting Minnesota jurisdictional reporting in the Company's Jurisdictional Annual Reports and associated explanatory footnotes.

The only area of disagreement is the depreciation of regulatory utility operations buildings. The Departments has requested that GP, in its next depreciation filing, include a schedule listing each of these buildings, including the account in which the building is booked, cost amounts, individual or allocated depreciation reserve amounts, depreciation rate and method, in-service date, building address/location, and description of the asset's operational purpose. Great Plains states that, since it uses a group depreciation basis in its Account No. 390 – General Structures and Improvements, providing this information on an individual asset basis would be complicated, particularly allocating the accumulated reserves. The Department has filed a supplemental response letter with the Commission expressing the importance of obtaining this data to properly evaluate the continued use of group depreciation accounting methods for utility service buildings.

The Department has made a similar request of MERC and Minnesota Power in other dockets.

## V. Decision Options

**Instant Petition**

1. Approve Great Plains Natural Gas Co.'s proposed 2018 Second Revised Depreciation Study, filed November 5, 2018. (Great Plains, DOC) OR
2. Do not approve Great Plains Natural Gas Co.'s proposed 2018 Second Revised Depreciation Study, filed November 5, 2018.

**In Great Plains' Next Depreciation Filing**

3. Provide a more robust analysis of the accounts affected by Great Plains' PVC replacement program. (DOC, GP does not object) AND
4. Direct Great Plains to provide a schedule listing all buildings used for regulated utility operations, including cost amounts, depreciation amounts, depreciation method and rate, placed-in-service dates, building address/location, building's operational purpose, and account where building is booked. (DOC)

**In Great Plains' Future Depreciation Filings**

5. Transparently disclose changes to its depreciation-study approach. (DOC) AND
6. Submit a full depreciation study if the Company alters its depreciation approach before its next scheduled 5-year depreciation filing. (DOC) AND
7. Provide activity schedules required by Minn. Rule 7825.0700 showing additions, retirements, adjustments, and transfers for plant-in-service accounts and their associated accumulated depreciation accounts. (DOC) AND
8. Require Great Plains to conduct a full depreciation study of any plant group with a change in the survivor curve prior to the Company's next scheduled 5-year depreciation study, or completely explain why a full study is not necessary. (DOC)

**Great Plains' Jurisdictional Annual Reports**

9. Direct Great Plains to report, in future Minnesota Jurisdictional Annual Report (JAR) filings, the Minnesota-jurisdictional amounts in the gas plant-in-service accounts; and order that in the Company's next JAR the 2018 beginning-of-year balances for the gas plant-in-service accounts reflect the jurisdictional amount, footnoted to explain the reason the 2018 beginning-of-year balances differ from the reported 2017 year-end balance in Great Plains Jurisdictional annual Report in Docket No. E,G-999/PR-18-04. (DOC)