MINNESOTA
PUBLIC UTILITIES COMMISSION

Staff Briefing Papers

Meeting Date	April 26, 2018		Agenda Item #1*
Company	Minnesota Energy Resources Corporation		
Docket No.	Docket No. G-011/D-17-442		
Issues	**In the Matter of** the Petition of Minnesota Energy Resources Corporation (MERC) for Approval of its 2017 Five-Year Review of Depreciation Certification Docket 1) Should the Commission approve MERC's 2017 five year depreciation certification study? 2) Should MERC be required to file its next remaining lives depreciation filing on June 1, 2018, or June 1, 2019?		
Staff	Ann Schwieger	Ann.schwieger@state.mn.us	651-201-2238

✓ **Relevant Documents**	**Date**
MERC – Initial Filing	May 31, 2017
Department – Comments	December 7, 2017
MERC – Response Comments	December 15, 2017

To request this document in another format such as large print or audio, call 651.296.0406 (voice). Persons with a hearing or speech impairment may call using their preferred Telecommunications Relay Service or email consumer.puc@state.mn.us for assistance.

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

I. Statement of the Issues

1) Should the Commission approve MERC's 2017 five year depreciation certification study?

2) Should MERC be required to file its next remaining lives depreciation filing on June 1, 2018, or June 1, 2019?

II. Background

May 31, 2017: MERC made its initial filing for approval of its 2017 five-year review of depreciation certification. MERC stated it anticipates filing a rate case in the near future with a 2018 test year and will incorporate the depreciation parameters decided in this case into its rate case calculations.

MERC stated that its review and depreciation analysis demonstrated the need to revise depreciation rates for asset classes. If the Commission were to approve MERC's proposed changes, the annual depreciation expense would decrease by approximately $1.24 million as compared to the currently approved rates. MERC requested the rates be implemented on January 1, 2017.

MERC uses functional composite depreciation rates for assets that are fully depreciated but may have future investment. MERC proposed the following changes to the composite depreciation rates. The effect on the depreciation expense is also shown:

Function	Currently Approved	Recommended	Change in Depreciation Expense
Transmission	2.91%	2.35%	($58,900)
Distribution	2.43%	2.13%	($1,292,318)
General	4.78%	5.36%	$109,868

MERC attributed the changes in expense to the following results of the study:

Transmission assets: The cost of removal of Transmission Mains (Account 367.1) is currently set at a negative 45 percent salvage rate. MERC has incorporated an additional five years of cost removal data and the study reflects a negative 30 percent net salvage value;

Distribution assets: The change in depreciation expense is attributable to the change in net salvage rates for Distribution Services (Account 380.0) and Distribution Mains (Account 376.0). The Distribution Services net salvage rate is currently set at negative 60 percent and MERC has proposed a net salvage rate of negative 55 percent. The Distribution Mains net salvage rate is currently set at negative forty-five percent and MERC has proposed a negative thirty percent net salvage rate.

General Plant: The increase in expense is attributable to the declining resale value of Transportation Equipment (Accounts 392.1 & 392.2). The current values are set at a positive twenty-five and thirty percent. The five-year study shows that the value has been reduced to a positive twenty-five and fifteen percent.

MERC listed major future additions or retirements to the plant accounts that the utility believes may have a material effect on the current certification results under Minn. R. 7825.0700. MERC stated it continues to experience an increased level of investment particularly in distribution mains, services, and station accounts resulting in increased plant additions as a result of regular system improvements.

MERC stated it will also experience an increased level of investment as a result of the approval of the Rochester Natural Gas Extension Project under Dockets G-011/M-15-895 and G-011/M-16-315.

<u>December 7, 2017:</u> The Department submitted comments and recommended that the Commission approve MERC's proposal. Based on its review. The Department noted that the proposed average service lives, net salvage values, and resulting depreciation rates are supported by the record and appear to be reasonable. The Department pointed out that the Commission's determination in depreciation proceedings are for accounting purposes only and not a determination for purposes of setting rates. The Department stated that due to MERC's pending rate case (G-011/GR-17-563), which appears to be largely capital driven, it will also review the depreciation lives related to capital investments in the rate case.

The Department recommended that the Commission determine the following:

- Require the next five-year study due by June 1, 2022;
- Require MERC to file its next annual remaining life update by June 1, 2018;
- Approve MERC's proposed lives and net salvage rates; and
- Approve MERC's proposal to continue use of functional composite depreciation rates.

<u>December 15, 2017:</u> MERC submitted reply comments and stated its agreement with the Department's recommendation that the Commission approve the Company's proposed lives and salvage values effective January 1, 2017.

MERC disagreed with the Department's recommendation that the Company file its next annual remaining life update by June 1, 2018. MERC stated that, due to the timing of the Commission's decision in the current docket, MERC will not have the parameters proposed on May 31, 2017 in place in its capital asset management system as of December 2017. This would result in the 2018 annual remaining life update using outdated information.

MERC stated that a similar situation occurred with the Company's 2012 depreciation study in Docket No. G-007, 011/D-12-533. In that case, the Company's proposed depreciation study was not yet approved at the time the 2013 annual remaining life update was due. To comply with the Commission's Order in Docket No. G-007, 011/D-11-491, MERC completed its annual update using depreciation parameters in effect at the time, but requested that the results of the update be disregarded as the Company's new study results would supplement the parameters used in that remaining life update. The Department and the Commission both agreed with MERC's proposal.

MERC stated it would like to avoid both the unnecessary time and expense to prepare an annual remaining life update in 2018 that is based on outdated information. MERC has asked the Commission to Order its next annual remaining life update to be due on June 1, 2019.

The Department did not issue response comments but instead verbally stated its agreement with MERC's proposal to change the due date to June 1, 2019.

III. Decision Options

1) The Department and MERC both recommended that the Commission approve the following:
    - Require the next five-year study due by June 1, 2022;
    - Approve MERC's proposed lives and net salvage rates; and
    - Approve MERC's proposal to continue use of functional composite depreciation rates.

2) Require MERC to file its next annual depreciation update on June 1, 2018.
   OR
3) Require MERC to file its next annual depreciation update on June 1, 2019. (MERC, Department)