

Remaining Lives Order as it addresses the Commission's concerns related to changes in remaining lives and the impacts of the changes on rates for customers.

Q. DO YOU RECOMMEND ANY CHANGES TO THE CURRENTLY-APPROVED REMAINING LIVES BASED ON THIS REVIEW?

A. Yes. We concluded there were either significant additions or other contributing factors for Prairie Island and Black Dog such that we recommend a change in remaining life as appropriate for this case. Each is discussed in greater detail below.

We also identified several facilities, specifically Blue Lake and Granite City, which may need modifications in our upcoming remaining life filing. These changes would not be significant if proposed. We are currently working with plant personnel on these but wanted to make sure parties were aware that they may be included in our February remaining life filing.

The summary of our analysis done in preparation for this filing is shown in Exhibit ___(LHP-1), Schedule 2.

1) Prairie Island

Q. WHAT SIGNIFICANT ADDITION HAS BEEN MADE TO THE PLANT INVESTMENT FOR PRAIRIE ISLAND?

A. As discussed more fully by Company witness Dennis Koehl, we are making significant investments at our Prairie Island nuclear power plant in anticipation of the Nuclear Regulatory Commission ("NRC") approving our applications for renewal of the operating licenses to extend both units'

operating lives until 2033 and 2034. The investments are required to ensure Prairie Island can continue to operate safely and effectively throughout the length of the renewed license. A large portion of this investment, almost \$68 million, is expected to be spent on the purchase of interim spent fuel storage casks, which will be required in order to properly and safely store the spent nuclear fuel that will be generated by the plants over the additional 20 years. A number of smaller, but still significant, projects are planned to upgrade and maintain the production units themselves.

Q. ARE THERE ANY CONTRIBUTING FACTORS THAT WOULD INFLUENCE YOUR REVIEW OF THE REMAINING LIFE FOR PRAIRIE ISLAND?

A. Yes, the main contributing factor that influences the Prairie Island remaining life is the pending application for renewal of the two NRC operating licenses, one for each unit. It is anticipated the NRC will grant the extension of these licenses by the end of the first quarter of 2011. The licenses are currently set to expire in August 2013 for Unit 1 and October 2014 for Unit 2. As noted above, we presume the renewal will be approved, thus extending the termination of the operating licenses out to August 2033 for Unit 1 and October 2034 for Unit 2. The Prairie Island remaining life is a composite based on the termination date of the two licenses.

Q. WHAT EFFECT DO THE ANTICIPATED LICENSE RENEWALS HAVE ON THE REMAINING LIFE OF PRAIRIE ISLAND?

A. Previously, the remaining life for Prairie Island was extended 10 years in anticipation of the Company receiving the license extension from the

NRC. This was initially reflected in final rates in our last electric rate case (Docket No. E002/GR-08-1065), and was approved through the 2010 Remaining Lives Order. This set the remaining life to 14.3 years as of January 1, 2010 based on an assumed extension out to 2023 for Unit 1 and 2024 for Unit 2. With the license extensions anticipated to be approved in 2011, the Company is requesting to extend the life an additional 10 years to reflect the full effect of the license extension effective January 1, 2011. Thus, the remaining life for Prairie Island would be 23.3 at January 1, 2011 based on the entire license extension to 2033 for Unit 1 and 2034 for Unit 2.

Q. WHAT IMPACT DOES THE REMAINING LIFE EXTENSION AT PRAIRIE ISLAND HAVE ON DEPRECIATION EXPENSE IN THE TEST YEAR?

A. The extension of the remaining life for Prairie Island will result in a decrease in the annual depreciation expense for the plant in 2011. Based on forecasted plant balances going forward, the estimated impact on depreciation is approximately \$12.1 million, this change is for total NSPM.

Q. DOES THIS LIFE CHANGE AFFECT ANY OTHER ITEMS INCLUDED IN REVENUE REQUIREMENTS FOR THIS RATE CASE?

A. There are two other expense items which are related to and affected by a remaining life change to Prairie Island. These two expenses are the accrual for the nuclear decommissioning and the accrual for end-of-life nuclear fuel costs.

Q. ARE THESE TWO EXPENSES TYPICALLY DETERMINED IN THE REMAINING LIFE FILING?

A. No. The extension of the remaining life for the Prairie Island units does not have a direct effect on the accrual periods for these components, since the accrual periods for decommissioning and end-of-life nuclear fuel are routinely established in different depreciation filings than those where the remaining lives are set. Currently, the accrual periods for these items correspond with the current remaining lives for the production units. For the sake of continuity, we propose that the accrual periods for both nuclear decommissioning and end-of-life nuclear fuel costs both be extended an additional ten years. As with the remaining life of the nuclear plant units, this would result in accrual periods which extend to 2033 for Prairie Island Unit 1 and 2034 for Unit 2.

Q. DOES THE EXTENSION OF ACCRUAL PERIODS FOR THE NUCLEAR DECOMMISSIONING AND END-OF-LIFE NUCLEAR FUEL COSTS AFFECT DEPRECIATION EXPENSE?

A. The extension of the accrual period for the nuclear decommissioning trust fund has no effect on depreciation expense. In the most recent Triennial Nuclear Decommissioning filing (Docket No. E002/M-08-1201), it was determined that the balance currently set aside in the nuclear decommissioning trust fund and escrow account would be sufficient enough to cover all estimated future decommissioning costs. Thus, the nuclear decommissioning accrual was set to zero beginning in 2009. A lengthening of the accrual period would not change this decommissioning accrual at this time.

Regarding end-of-life nuclear fuel costs, the lengthening of the accrual period allows for recovery of the estimated costs over an additional 10

years. This simply extends the life over which the cost of the unburned nuclear fuel at the time of shutdown of our nuclear generating units is depreciated. The result of the change in remaining life produces a decrease in annual depreciation expense of \$908 thousand. The change in the depreciation expense, for the production asset and the end-of-life nuclear fuel, results in a total change of approximately \$13.0 million for Prairie Island for total NSPM.

Q. ARE THERE ANY OTHER CONSIDERATIONS REGARDING NUCLEAR DECOMMISSIONING BESIDES THE CHANGE TO REMAINING LIFE THAT YOU ARE CONSIDERING?

A. Yes. Previously, when Monticello received approval for license extension, we conducted a full decommissioning review and concluded that the decommissioning trust fund was over funded for the foreseeable future and that amounts paid into escrow were appropriately eligible for refund. As we near the triggering event of NRC approval, in regard to the Prairie Island escrow and the possibility for amounts in escrow to be refunded, we are evaluating key component assumptions. Our stress test of Monticello focused primarily on the risk of a depletion of the decommissioning fund from the potential of a disruptive market loss. Based on today's circumstances, we are now, evaluating how certain other key components, such as the potential of a lower real growth rate and a lengthened period for full removal from the site may impact the fund. We are in the very early stages of preparing this additional information, thus it would be premature to draw conclusions regarding a potential refund at this time. As we continue to refine this analysis, we will provide additional

information as it becomes available, culminating in a full triennial review in October.

Q. HAVE THE CHANGES DESCRIBED ABOVE BEEN INCORPORATED INTO THE RATE CASE DATA?

A. Yes. The changes discussed for Prairie Island has been incorporated into the final revenue requirement proposed by the Company in this case.

2) *Black Dog*

Q. WHAT SIGNIFICANT CHANGES ARE PLANNED FOR THE OPERATION OF BLACK DOG?

A. In the Company's 2010 Resource Plan, we discussed the future plan of operations at Black Dog. While the output of Units 3 and 4 is important to maintaining system reliability, Units 3 and 4 are only expected to be able to operate for a few more years without significant upgrades to environmental controls and other equipment. After extensive study, we determined the most cost effective solution was to construct a new combined-cycle unit on the site of the plant's current coal field and take Units 3 and 4 off-line once the new unit is in-service. This plan calls for Units 3 and 4 to cease using coal as fuel in 2013 to allow for construction to begin on a new Unit 6, but to continue providing electric production using natural gas as needed until Unit 6 is in-service, which is expected to be early 2016.

Q. WHAT EFFECT DOES THE PLAN FOR BLACK DOG REPOWERING TO A NEW UNIT 6 HAVE ON THE REMAINING LIVES FOR BLACK DOG UNITS 3 AND 4?

A. Currently, the approved remaining life for Black Dog is set to run until the end of 2012. Under the plan described above, these units would continue production until Unit 6 is in-service, which is expected to be sometime in early 2016. To account for this, the Company is proposing that the remaining life for Black Dog be extended 3 years, until the end of 2015. Therefore, Black Dog's remaining life would be 5 years at January 1, 2011.

Q. DOES THE PROPOSED CHANGE PRESUME THAT THE COMMISSION WOULD APPROVE A CERTIFICATE OF NEED FOR THE REPOWERING OF BLACK DOG?

A. No. The three-year life extension is consistent with our 2010 Resource Plan. The Commission will review and approve the best option for Black Dog in the Resource Plan proceeding. Given our analysis of the situation, we believe the three-year extension is appropriate to keep Black Dog operating through 2015. If the Commission determined that repowering was not an appropriate path, the Company would evaluate the impact of this decision on the next Remaining Life filing and propose any further changes at that time. We believe this extension is appropriate, without prejudging the merits of the Company's 2010 Resource Plan or any future Certificate of Need filing.

Q. DID YOU REVIEW THE EXPECTED REMOVAL COSTS FOR BLACK DOG?

A. Currently, Black Dog uses a net salvage rate of negative 18 percent as approved in the 2010 Remaining Lives Order. In our 2010 Review of Remaining Lives filing, the Company presented an updated dismantling study for the electric steam and other production units. The estimates for final removal are not available at this time. Although this study was fairly

current, the Company did investigate whether the current estimate was still viable. The current estimate was reviewed with various Energy Supply experts familiar with Black Dog. It was concluded that the amount provided in the dismantling study is at least sufficient and could be less than what the dismantling will actually cost. However, given the fact that the numbers are not yet developed, we did not recommend any change to the estimate provided in the 2010 Review of Remaining Lives filing. We anticipate more information will be known in 2011 if we receive approval for the repowering and, if so, the new information will be provided with the 2012 Remaining Lives filing.

Q. WHAT IMPACT DOES THE LIFE EXTENSION FOR BLACK DOG UNITS 3 AND 4 HAVE ON DEPRECIATION EXPENSE IN THIS CASE?

A. The impact on this proceeding by lengthening the life three years is a proposed decrease in depreciation expense of \$9.5 million beginning January 1, 2011 for total NSPM.

Q. HOW HAVE THE CHANGES BEEN INCORPORATED INTO THE RATE CASE DATA?

A. The changes discussed for Black Dog Units 3 and 4 have been incorporated into the final revenue requirement proposed by the Company.

III . DEPRECIATION USING MINNESOTA RULES

Q. HAVE YOU CALCULATED THE DEPRECIATION EXPENSE IN THIS CASE USING THE LIVES AND RATES AS APPROVED BY THE COMMISSION?

A. Yes. The depreciation expense included in rate case data begins with the lives and rates currently approved by the Commission. Any changes to those approved lives are calculated as adjustments to the base data and added to the expense calculated using approved lives and rates. The approved lives and rates are referred to as the calculation based on “Minnesota Rules” within the Company.

Q. WHY IS THIS IMPORTANT TO NOTE?

A. Prior to 2009, the North Dakota and South Dakota Commissions have used the same depreciation lives and rates that were approved by this Commission. Thus, the financial depreciation expense and accumulated depreciation could be used as the starting point for jurisdictional allocation. In 2009, the North Dakota and South Dakota Commissions deviated from past practice and set depreciation lives and rates different than what was authorized by this Commission. The financial depreciation and accumulated depreciation from 2009 forward represented a composite of all the approved rates weighted by jurisdictional percentages. In order to stay true to the statement that the depreciation lives and rates approved by this Commission, or Minnesota Rules, were used for the rate case data, the Company began tracking a depreciation expense and accumulated depreciation for Minnesota jurisdiction, albeit at total NSPM level, beginning with January 1, 2009. The separate depreciation expense and accumulated depreciation were calculated each month using Minnesota Rules. The same calculation was done for North Dakota and South Dakota using their approved lives and rates, again at total NSPM. The financial depreciation was calculated using the current jurisdictional percentages applied to the monthly depreciations calculated using the various state rules. The

financial accumulated depreciation was rolled forward each month using the financial depreciation.