

1 approaches.

2 JUDGE DIPPELL: This is sounding
3 more and more like an objection, Mr. Pendergast.

4 MR. PENDERGAST: For example, she
5 references -- on page 6, she talks about
6 development of recommended net salvage ratios by
7 depreciation of consultant L.W. Loos in Empire
8 District Electric Company rate case and goes on to
9 reference what the recommendations were there.
10 She talks on page 7 about Missouri Gas Energy and
11 what recommendations were there.

12 And all I'm suggesting is that when
13 it comes to references of that nature, if you were
14 to make some kind of determination that -- that
15 depreciation experience and recommendations
16 related to other utilities is not relevant, that
17 that ought to be subject to that same kind of
18 finding.

19 JUDGE DIPPELL: All right, then --

20 MR. SCHWARZ: If I might respond. I
21 think that the specific items to which Mr.
22 Pendergast has called the Commission's attention I
23 think are more akin to the suggestions, for
24 instance, that -- of general patterns. That is,
25 it's not -- it's not -- certainly not hearsay

1 because it's not offered for the truth of the
2 matter asserted.

3 I think that to the extent that the
4 objections to the Ameren UE data trends and Ameren
5 UE data are directed at what is an appropriate
6 depreciation rate for Laclede Gas Company, that
7 that's the basis of the objection to those
8 exhibits. This is more on the order of yes, there
9 are people who use approaches other than the
10 standard approach.

11 I think the purpose for which this
12 is offered is far different from the purposes of
13 the Ameren UE data to which --

14 JUDGE DIPPELL: I understand that.
15 I think what I'm going to do is treat this just
16 like I did the others and rule on it at the same
17 time, and I'll let Mr. Pendergast put his specific
18 objections in writing --

19 MR. PENDERGAST: Thank you, Your
20 Honor.

21 JUDGE DIPPELL: -- because I believe
22 he has the same -- he has a relevance objection is
23 what he's getting at. It may be very well
24 different objection, but I'm not going to take the
25 time right now to go through line by line Ms.

1 Schad's testimony.

2 So, again, we'll -- we will not -- I
3 will not admit that one at this time. I will
4 treat it, again, as an offer of proof. We'll go
5 ahead and have the cross examination, and I'll
6 rule on that after seeing those in writing.

7 Is there cross examination from the
8 Public Counsel?

9 MS. O'NEILL: No.

10 JUDGE DIPPELL: Ameren UE?

11 MR. LOWERY: Yes, Your Honor.

12 JUDGE DIPPELL: And I will remind
13 Counsel that there was some highly confidential
14 information in Ms. Schad's testimony. If -- if it
15 becomes necessary, please speak up, let me know
16 what that information might be so that we can go
17 in camera, if needed.

18 CROSS EXAMINATION BY MR. LOWERY:

19 Q Good morning, Miss Schad.

20 A Good morning.

21 Q You've read the prefiled
22 supplemental testimony of the other witnesses in
23 this case; is that correct?

24 A Yes.

25 Q And you've attended the depositions

1 of all of the witnesses in the case?

2 A Yes.

3 JUDGE DIPPELL: Miss Schad, I'm
4 going to need you to speak into the microphone.
5 Pull it closer to you, if you need to.

6 THE WITNESS: Okay.

7 Q (BY MR. LOWERY) It's my
8 understanding that you have adopted Mr. Adam's
9 testimony in this proceeding. Is that correct?

10 A Correct.

11 Q You've adopted the approach that he
12 took in this case to dealing with net salvage.
13 Correct?

14 A Correct.

15 Q Though you've never before submitted
16 testimony that endorses Mr. Adam's particular
17 method of dealing with net salvage; is that
18 correct?

19 A Correct.

20 Q All of your testimony over the last
21 few years on this issue recommends removing net
22 salvage from the depreciation calculation entirely
23 and treating it as an expense. Is that fair?

24 A Yes.

25 Q At your deposition you testified

1 that there really isn't much difference between
2 the approach you support personally and Mr. Adam's
3 approach. Do you recall that?

4 A Correct.

5 Q And Mr. Oligschlaeger, I believe he
6 testified in his deposition that substantively the
7 two approaches are identical. Do you recall that?

8 A Yes.

9 Q I want to make sure that you and I
10 are on the same page about a couple of things.
11 Under the standard approach, what the depreciation
12 analyst does is he or she looks at the data in a
13 particular plant account, let's use gas mains
14 because that's one of Laclede's biggest accounts;
15 is that fair?

16 A Except for the fact that the Staff
17 does not have a concept called standard.

18 Q Well, when I use the term "standard
19 approach," you understand that I'm talking about
20 -- or just for purposes of my questions, would you
21 just agree that I'm talking about the approach
22 that's been recommended in the Company's
23 testimony?

24 A And would you explain that approach?
25 So that I'm sure that I'm clear?

1 Q The standard approach -- well, the
2 standard approach, as I am using it, is an
3 approach where the historical ratio of the cost to
4 retire a particular plant, a particular account,
5 is related to the original cost of that retired
6 plant to arrive at a net salvage percent, and that
7 percent has been used in the traditional whole
8 life formula.

9 A And over what number of years is
10 that applicable?

11 Q Have you read Mr. Stout's testimony?

12 A I'm asking -- so I know exactly how
13 you want me to use it.

14 Q The number of years would vary
15 depending on what the average service life of the
16 account is, of course. You understand that,
17 correct?

18 A That's how you vary it, according to
19 the average service life of the account? That's
20 how I am to take it? And use it in this example?

21 Q I'm not -- I'm not using it in this
22 example. Let me -- let me just ask this question.
23 Under the approach I just described, the
24 depreciation analyst determines the ratio of costs
25 of removing or retiring the plant in that account

1 to the original cost of the retirements in that
2 account. Is that correct?

3 A Only if I know of number of years
4 for doing so.

5 Q Well, I'm not asking you about a
6 particular depreciation rate or a particular
7 number of years.

8 A I understand, but if I'm going to
9 take a ratio, I need to know if I'm going to do
10 just one year or five years, 20 years, I need to
11 know what is the hypothesis of this. What am I
12 assuming so that I can continue to answer the
13 question.

14 Q I'm not asking you --

15 A It does make a difference, so I have
16 to know.

17 Q Miss Schad, I think it's my job to
18 ask you questions and you to answer those
19 questions. It's not to ask me questions.

20 A I understand. Okay.

21 Q In terms of determining the net
22 salvage percent itself, not the depreciation rate
23 associated with net salvage, but the net salvage
24 percent itself, you take the ratio of costs of
25 removing or retiring the plant in that account and

1 you relate that to the original cost of the plant
2 retired. That's the approach that Mr. Stout
3 takes; is that correct? That your understanding?

4 A Yes.

5 Q And that ratio produces a net
6 salvage percent.

7 A Yes.

8 Q And that net salvage percent is
9 often negative for a utility plant. True?

10 A True.

11 Q It's often negative because the cost
12 to remove or retire the plant is often greater
13 than any salvage that can be realized from
14 selling, for example, the scrap iron or scrap
15 steel from a gas main.

16 A Yes.

17 Q And as with all statistical analyses
18 after you do those calculations, the depreciation
19 analyst may apply judgment to come up with exactly
20 what net salvage percentage he or she uses in the
21 depreciation calculation. Is that fair?

22 A Well, at that point I haven't done a
23 statistical analysis. I've taken a ratio.

24 Q After that ratio is determined, the
25 depreciation analyst may apply judgment in terms

1 of actually the percent that he or she actually
2 uses in calculating depreciation rate. Is that
3 fair?

4 A Yes.

5 Q Now, in order to derive the
6 depreciation rate to the original plant in service
7 under that approach, once the analyst calculates
8 that initial ratio we just talked about and then
9 he or she may or may not apply judgment to adjust
10 that percentage, the net salvage percent is then
11 divided by the estimated average service life of
12 the plant in that account, whatever that service
13 life may be. Correct?

14 A Yes.

15 Q You've previously submitted
16 testimony in cases before this Commission in which
17 you indicate that you also must use your judgment
18 to estimate average service lives. Correct?

19 A Yes.

20 Q So judgments applied in determining
21 average service lives, right?

22 A Yes.

23 Q And you've previously also testified
24 in other Commission cases that average service
25 lives are dynamic and they may change over time.

1 A Yes.

2 Q Is it fair, then, to say that
3 there's more to estimating average service lives
4 than simply inputting data into a computer program
5 and then getting a printout from that program that
6 tells you exactly what that service life is going
7 to be?

8 A Is there more than --

9 Q If you input data into the Gannett
10 Fleming software that the Staff uses, for example,
11 and you get a printout, that doesn't necessarily
12 tell you the average service life that you will
13 adopt for that account, is that correct?

14 A That is correct.

15 Q You use judgment and several
16 factors, you take several things into
17 consideration in coming up with what you think the
18 average service life for that account should be?

19 A Yes.

20 Q Now, getting back to estimates of
21 net salvage versus estimates of service lives, if
22 we take that account, gas main account, for
23 example, the net salvage calculation, the net
24 salvage percentage, that ratio I described just a
25 minute ago plus any informed judgment applied by

1 the analyst, that's going to give us the net
2 salvage component of the depreciation rate for gas
3 mains, right? And if you assume a service life.

4 A Okay.

5 Q Correct?

6 A Yes.

7 Q You've indicated in your
8 supplemental rebuttal testimony that what the
9 standard approach seeks to do is to estimate the
10 future cost of removing or retiring the assets and
11 then ratably recover that cost over the service
12 lives of the plant at issue. Do you recall that
13 testimony?

14 A Yes.

15 Q Now, under the standard approach,
16 the analyst is not trying to figure out what past
17 removal or retirement costs were, correct?

18 A Under the --

19 Q Under the standard approach.

20 A Am I looking -- am I -- ask me the
21 question again.

22 Q You indicated what you believe the
23 standard approach seeks to do in your supplemental
24 rebuttal testimony, and what you said was that it
25 seeks to estimate the future net cost of removing

1 or retiring the assets and then it seeks to
2 ratably recover that cost over the service life of
3 the plant at issue. That was your testimony.

4 Correct?

5 A Okay.

6 Q Under the standard approach that you
7 described, the analyst is not trying to figure out
8 what past removal or retirement costs were.

9 Correct?

10 A That is not correct. How am I going
11 to develop a ratio without it?

12 Q The ratio is a ratio derived from
13 historical data, correct?

14 A That's what I'm saying. I have to
15 have historical data. I have to know what it is.

16 Q That's true. The historical data is
17 necessary to calculate the ratio we just
18 discussed. Right?

19 A Yes.

20 Q That ratio is seeking to predict
21 what the future net salvage costs are going to be
22 for the plant in service in that account; is that
23 right?

24 A Yes.

25 Q It's not seeking to predict what the

1 costs were in the past.

2 A It is using the past.

3 Q It's using the past, but it's not
4 seeking to predict what those costs will be. We
5 already know what costs were in the past, do we
6 not?

7 A Yes.

8 Q So it's not seeking to predict those
9 costs again, it's seeking to predict what the net
10 salvage costs are going to be in the future.

11 A Okay.

12 Q Correct?

13 A Correct.

14 Q In your supplemental rebuttal
15 testimony at page 6, you cite a passage from the
16 NARUC depreciation practices publication.

17 A Okay.

18 Q Do you not?

19 A Yes.

20 Q And you cited, I believe, a support
21 for what appears to be your contention that there
22 really is no, quote, standard approach to net
23 salvage. Is that the basic point that you were
24 trying to make?

25 A In conjunction with my experience

1 that has told me it is not.

2 Q But in citing the NARUC passage,
3 that was complementary of what you say is your
4 experience that it's not. Is that -- is that
5 fair?

6 A Yes.

7 MR. LOWERY: May I approach the
8 witness?

9 JUDGE DIPPELL: Yes.

10 Q (BY MR. LOWERY) I'm going to hand
11 you a copy of the NARUC publication I was just
12 referring to. You're familiar with that
13 publication. Correct?

14 A Yes.

15 Q Would you turn to page 18? You see
16 the heading that says, Salvage Considerations?

17 A Yes.

18 Q Would you read the first paragraph
19 on page 18 into the record?

20 A Under presently accepted concepts,
21 the amount of depreciation to be accrued over the
22 life of an asset is its original cost less net
23 salvage. Net salvage is the difference between
24 the gross salvage that will be realized when the
25 asset is disposed of and the cost of retiring it.

1 Positive net salvage occurs when
2 gross salvage exceeds cost of retirement, and
3 negative net salvage occurs when cost of
4 retirement exceeds gross salvage. Net salvage is
5 expressed as a percentage of plant retired by
6 dividing the dollars of net salvage by the dollars
7 of original cost of plant retired.

8 The goal of accounting for net
9 salvage is to allocate the net costs of an asset
10 to accounting periods making due allowance for the
11 net salvage, positive or negative, that will be
12 obtained when the asset is retired.

13 This concept carries with it the
14 premise that property ownership includes the
15 responsibility for the property's ultimate
16 abandonment or removal. Hence, if current users
17 benefit from its use, they should pay their pro
18 rata share of the cost involved in the abandonment
19 or removal of the property, and also receive their
20 pro rata share of the benefits of the proceeds
21 realized.

22 Q Thank you. The first sentence you
23 read in that paragraph, clearly net salvage is a
24 part of the depreciation calculation under the
25 presently accepted concepts described in that

1 paragraph, is it not?

2 A That's what it states.

3 Q And while you contend that that
4 remains true in Mr. Adam's approach, it's not true
5 in the approach that you've personally recommended
6 several times, is it?

7 A Correct.

8 Q Let's take a look in particular in
9 the fourth sentence in that paragraph that you
10 just read. That fourth sentence describes
11 precisely the standard method of estimating net
12 salvage percentages that Mr. Stout describes in
13 his testimony, does it not?

14 A Yes.

15 Q And that statement is in the
16 paragraph in this publication from the National
17 Association of Regulatory Utility Commissioners
18 describing the presently accepted concepts; is
19 that not true?

20 A Yes.

21 Q The net salvage percentage utilized
22 by Mr. Adam in his recommended depreciation rates
23 in this case did not utilize that ratio described
24 in that sentence, did it?

25 A No.

1 Q He, in fact, started out calculating
2 the net salvage percent in that way, but he took
3 some additional steps that ultimately resulted in
4 him changing the net salvage percentage that he
5 had originally calculated. Is that your
6 understanding?

7 A Yes.

8 Q And the additional steps he took are
9 not reflected in the methodology described in the
10 fourth sentence of that paragraph you just read,
11 are they?

12 A No, they are not.

13 Q And the reason he took those
14 additional steps is because he was trying to
15 approximate the actual net salvage experience for
16 the particular account he was looking at in the
17 recent past. Correct?

18 A That is correct.

19 Q So while the NARUC publication, as
20 you point out in your testimony, recognizes that
21 some commissions have abandoned what we are
22 referring to as the standard approach, that very
23 same publication recognizes that the standard
24 approach to calculating the net salvage
25 percentages is the presently accepted approach,

1 **does it not?**

2 A It does. However, in this date, in
3 1999, our engineers did not use this formula, and
4 that is what the Commission ordered, accepted in
5 that case, ER-90-101.

6 Q Would you turn to page 318 of the
7 **NARUC Public Utility Depreciation Practices**
8 **publication? Do you see the definition of**
9 **depreciation there?**

10 A Yes, I do.

11 Q And that's the glossary in this
12 **publication, correct?**

13 A Yes, it is.

14 Q Could you read that definition into
15 **the record, please?**

16 A As applied to the depreciable plant
17 and utilities, the term "depreciation" means the
18 loss in service value not restored by current
19 maintenance incurred in connection with the
20 consumption or prospective retirement of utility
21 plant in the course of service from causes that
22 are known to be in current operation against which
23 the company is not protected by insurance and the
24 effect of which can be forecast with reasonable
25 accuracy.

1 Among causes to be considered are
2 wear and tear, decay, action of the elements,
3 inadequacy, obsolescence, changes in the art,
4 changes in demand, and the requirements of public
5 authorities.

6 Q That definition is essentially the
7 same definition as appears in the uniform systems
8 of account. Is that fair? Do you need to see the
9 uniform systems of account definition?

10 A They are comparable.

11 Q When you say, "comparable," would it
12 be fair to say they're quite similar?

13 A Yes.

14 Q And NARUC recommends uniform systems
15 of account, does it not?

16 A The key there is recommends. It
17 does not require.

18 Q Would you turn to page 14 of the
19 NARUC publication?

20 A Okay.

21 Q I'm looking at the sentence starting
22 the uniform system of accounts in, I guess it
23 would be the first full paragraph after that
24 indented quote. Do you see that? Let me just --

25 MR. LOWERY: May I approach the

1 witness?

2 JUDGE DIPPELL: Yes.

3 Q (BY MR. LOWERY) I'm right here.
4 Starting right here. The NARUC publication
5 provides as follows on page 14. The uniform
6 system of accounts for electric utilities
7 recommended by NARUC defines service value as
8 follows, colon, the difference between the
9 original cost and the net salvage of the utility
10 plant. Did I read that accurately?

11 A Yes.

12 Q And then it goes on to say, quote,
13 "Loss in service value," end quote, therefore must
14 be understood and construed in light of its
15 specially defined meaning. Did I read that
16 accurately?

17 A Yes.

18 Q So the NARUC publication instructs
19 that one must understand service value in light of
20 how it is defined in the uniform system of
21 accounts. Correct?

22 A And am I to take this under the
23 reference to the electric utilities or to include
24 gas as well in this --

25 Q Is there a material difference?

1 Between the uniform system of accounts for gas
2 utilities or electric utilities for this -- with
3 respect to this particular point?

4 A I would not think so.

5 Q There isn't, is there?

6 A There are some differences in what
7 we have to look at when we do our work that's
8 electric versus gas.

9 Q But in terms of the definitions of
10 service value, net salvage, cost of removal,
11 depreciation, there's no material difference
12 between the gas uniform systems of account or the
13 electric uniform system of accounts; is that fair?

14 A That's fair.

15 Q And the specially defined meaning of
16 service value does take net salvage into account,
17 does it not?

18 A And I think the key there is that it
19 is a net salvage. This is a reference to concepts
20 where salvage is positive. If they wanted to say
21 net cost of removal, they would have said it.

22 Q On what do you base your contention
23 that a reference to net salvage only refers to
24 positive net salvage?

25 A Because if I want it to be negative,

1 I'll say net cost of removal.

2 Q Well, let's take a look at the
3 uniform system of accounts. Which version do you
4 have there? Gas or electric?

5 A I have gas.

6 Q Uniform system of accounts defines
7 net salvage as follows. And you correct me if I
8 read it incorrectly. I'll give you a moment to
9 get there. Net salvage value means the salvage
10 value of property retired less the cost of
11 removal. Did I read that accurately?

12 A You did.

13 Q So net salvage takes into account
14 cost of removal.

15 A It does.

16 Q And I won't read all of this, but if
17 we look at the definition of cost of removal,
18 which is, I believe, definition 10, cost of
19 removal means the cost of demolishing,
20 dismantling, tearing down or otherwise removing,
21 in this case, gas plant. Is that accurate?

22 A Yes.

23 Q There's no distinction made in these
24 definitions as to whether or not the salvage is
25 going to be positive or negative. That's a

1 calculation that has to be done with respect to a
2 particular account, does it not?

3 A It is a calculation, and if they had
4 wanted to do it, they could.

5 Q In your opinion.

6 A In my opinion.

7 Q In any event, the method for
8 calculation of depreciation rates that you
9 personally recommended consistently over the last
10 three or four years does not include a factor in
11 the depreciation rate calculation for net salvage;
12 correct?

13 A That is correct.

14 Q Could you turn to page 43 of the
15 NARUC publication? Are you there?

16 A Yes.

17 Q Would you please read the second
18 full paragraph starting up why operational into
19 the record?

20 A Why operational assets give rise to
21 an expense each accounting period can be best
22 understood if the investment in operational asset
23 is viewed as a prepaid expense. An operational
24 asset is acquired for use over a number of years.
25 Moreover, it is known at the outset that the asset

1 has a finite useful life and that the value of the
2 asset will be substantially diminished at the end
3 of its useful life.

4 The decline in the value of the
5 asset during its useful life is an expense of
6 operations related to the entire period.
7 Depreciation accounting estimates the expense
8 based -- I'm sorry. Depreciation accounting
9 estimates that expense based on life and salvage
10 estimates and allocates a portion of expense to
11 each accounting period.

12 Q That last sentence, let me read it
13 and see if you agree. Depreciation accounting
14 estimates that expense based on life and salvage
15 estimates and allocates a portion of the expense
16 to each accounting period. Did I read that
17 accurately?

18 A You read it accurately.

19 Q So NARUC, in the paragraph that you
20 just read, it recognizes that salvage estimates
21 are used, that the estimates of salvage are part
22 of the expense of the asset, and that one
23 allocates that expense to the life of the period
24 of the asset. Is that what that says?

25 A It said to me that the asset has a

1 finite useful life, and when I'm referring to a
2 mass property characteristic, according to what's
3 in NARUC, it has told me that mass property
4 characteristic has no definite overall life or
5 planned final retirement date.

6 Q I don't believe that answered my
7 question, though, did it?

8 A Well, if I'm going to go to that
9 step, I have to assume the sentence before that is
10 appropriate and accurate.

11 Q You may have lost me. Are you
12 contending the sentence before that's accurate or
13 inaccurate?

14 A Well, if I have the -- if I'm going
15 to allocate a portion of that expense of that
16 asset, then the asset has to be what we're talking
17 about here, which is a -- the asset has a finite
18 useful life. And we're talking about mass assets
19 in this -- in this, but yet a mass asset, if I'm
20 going to apply this to what I'm using it for, a
21 mass asset has no definite overall life.

22 Q Are you saying that, for example, I
23 think it's account 376, which is gas mains for
24 Laclede, that in depreciation calculations that
25 are done, there's no average service life assumed

1 for that account?

2 A That's not what I said. I said we
3 do not have a finite.

4 Q But this paragraph recognizes that
5 salvage estimates are used. Does it not?

6 A In the context of the paragraph. Is
7 there in the --

8 Q In the context of the paragraph,
9 whatever it is, it does recognize that salvage
10 estimates are used, does it not?

11 A Yes.

12 Q Estimates are used. And also
13 recognizes estimates of salvage are part of the
14 expense of the asset. Correct?

15 A Yes.

16 Q And it recognizes that you allocate
17 that expense to each accounting period over the
18 entire life of the asset. Whatever that is.
19 Right?

20 A Yes. Yes.

21 Q Now, if you expense net salvage as
22 you personally recommended in many cases, you
23 don't use those estimates, do you?

24 A I do -- we do use a estimate,
25 placeholder, in the rate cases when we expense the

1 net salvage.

2 Q At most, you're trying to estimate
3 what the expense might be for the period of the
4 rate case, maybe three, four, five years; is that
5 correct?

6 A That is our objective.

7 Q At most, that's what you're doing.
8 You're trying to estimate what the actual net
9 salvage costs may be 30, 40, 50 years from now.

10 A It is what we do. It is the
11 objective of our work in the rate case.

12 Q I understand that. But your
13 objective is not to estimate what the actual costs
14 are going to be 30 or 40 or 50 years later.
15 You're only trying to use those past costs that
16 you look at, whether it's over a three year
17 period, five year period, whatever, and you're
18 attempting to use that as a proxy for the short
19 term; correct?

20 A That is correct.

21 Q Calculation of net salvage according
22 to Mr. Adam's approach does not include any factor
23 to take into account growth in the plant or
24 inflation, correct?

25 A I did not see a factor in his for

1 inflation, although, as I said before, I would not
2 do every step the way he did, but there is always
3 a fine tuning of perhaps how I would do it, how
4 would you trend it. The conclusion that he came
5 to, as I said in my deposition, I don't have a
6 problem with. If I'm going to have some minute
7 changes, some small changes, that's probably
8 something that I would have considered.

9 Q But he didn't consider inflation as
10 a factor in making his calculation?

11 A No, he did not.

12 Q Historically we have seen inflation,
13 have we not?

14 A Yes.

15 Q You've testified in your deposition
16 that the net salvage costs over the five years
17 preceding this case are associated with a plant
18 that's no longer in service; is that right?

19 A That is correct.

20 Q A moment ago we talked about the
21 fact that the NARUC publication described the
22 method Mr. Stout uses in calculating the net
23 salvage percent. Do you remember that discussion?

24 A Yes.

25 Q You've known Laclede and Ameren UE

1 Witness Bill Stout for about five years?

2 A Yes.

3 Q And you know Mr. Stout because he
4 was one of the instructors at depreciation
5 training and seminars that you've attended.
6 Correct?

7 A Yes.

8 Q You've never served as an instructor
9 at such training, have you?

10 A No.

11 Q And you also know Mr. Stout because
12 he's President of Gannett Fleming, Inc., which is
13 the company that supplies the software to both
14 Staff and other Ameren utilities uses, correct?

15 A Yes.

16 Q And also because he's provided
17 expert testimony before this Commission in Case
18 No. WR-2000-844. Correct?

19 A Yes.

20 Q You've testified at your deposition,
21 have you not, that you have no opinion on whether
22 or not this Commission was correct when it
23 followed the standard approach in the St. Louis
24 County Water case, right?

25 A I hope that -- and maybe I need to

1 rephrase if I said it wrong. Their opinion, their
2 order in that is not something that I would have
3 an opinion on as to the appropriateness of it
4 because that is not my job.

5 Q You don't have an opinion -- I think
6 you just said the same thing. You don't have an
7 opinion about whether their order was appropriate
8 or not appropriate.

9 A No.

10 Q The Commission did agree in that
11 case, did they not, with the depreciation rate
12 suggested by Mr. Stout using the standard approach
13 as he describes it in his testimony?

14 A Let me try -- should I read it so I
15 know for sure how --

16 Q Do you know?

17 A My -- what I thought I read was that
18 the Commission said they could accept either one.

19 Q The Commission said they could
20 accept either method, but the depreciation rates
21 themselves, the rates, 3 percent, 4 percent,
22 whatever, that were adopted were under the
23 standard approach recommended by Mr. Stout.
24 Correct?

25 A That is correct.

1 Q You testified at your deposition
2 that you could not say whether Mr. Stout is
3 recognized nationally as an expert in
4 depreciation; right?

5 A I can say, although I will add to
6 that if he's testified in Missouri, we would
7 recognize him as an expert here.

8 Q But you couldn't say whether he was
9 recognized nationally, correct?

10 A Correct.

11 Q And, in fact, you've testified you
12 are not sure who is and who is not a recognized
13 national depreciation expert because there's no
14 board of any kind that actually certifies people
15 as such. Is that your testimony?

16 A There is no authority to give a
17 board the authority.

18 Q There's no authority -- there's no
19 board that certifies somebody as a nationally
20 recognized expert?

21 A I didn't say there's not someone
22 that doesn't certify, I said there's no authority
23 to give the board the authority to certify.

24 Q So without an authority that gives a
25 board the authority to certify somebody, that's

1 why you can't really, in your mind, recognize any
2 particular person as a nationally recognized
3 expert; is that right?

4 A That's -- that's how I feel.

5 Q And under that criteria, you
6 testified, for example, that you didn't know
7 whether Barry Bonds is a nationally recognized
8 baseball player; is that right?

9 A That is correct.

10 Q Do you recognize him?

11 A Well. I have been so fortunate
12 since that time to turn on a television in St.
13 Louis and see his name and see his name in my
14 business law book. So I would say I've -- I've --
15 I've gotten my --

16 Q If we asked you about George Brett,
17 you might have given a different answer? You're a
18 Royals fan, right?

19 A I do know who George Brett is.

20 Q In any event, you didn't name any
21 nationally recognized experts that endorsed the
22 Staff's approach at your deposition, correct?

23 A I did not at that time, but I would
24 -- I could at this time.

25 Q Seems like that's going to be

1 difficult unless there's an authority that gives a
2 board authority to certify somebody, but --

3 A Well, in Missouri, I would say --

4 Q There's no question pending.

5 A Um, can I comment?

6 Q I don't think there's a question
7 pending. That's up to Judge Dippell, but I don't
8 believe there's a question pending.

9 JUDGE DIPPELL: We'll just let Miss
10 Schad answer questions that are asked.

11 Q (BY MR. LOWERY) We discussed a
12 minute ago that you attended some training or
13 seminars on depreciation where Mr. Stout was an
14 instructor. Do you recall that?

15 A Yes.

16 Q And you testified at your deposition
17 that you don't remember what the instructors at
18 that training had to say about how net salvage
19 should be determined. Correct?

20 A I do not recall the very specifics
21 that they would have said.

22 Q Do you have a copy of your
23 deposition?

24 A Yes.

25 Q I'm looking at page 29, line 21.

1 Question: I guess what I'm asking
2 is, do you remember what the people who taught the
3 classes at Depreciation Programs, Inc., said was
4 the way to do it?

5 Answer: No. I mean, the idea is
6 that you just want to make sure that on
7 depreciation, you have recovered the full amount
8 which is the original cost, and then to the extent
9 that you don't want to have more than that, you
10 can have an adjustment called net salvage.

11 Question: Sure. And I mean, this
12 is kind of an aside from the merits of what's the
13 appropriate one to use and I know we've made --
14 we've heard arguments on both sides. I just want
15 to know if you remember, and maybe the answer is
16 you just don't remember.

17 And you answered no.

18 That was your testimony at your
19 deposition. Correct?

20 A Yes.

21 Q Since you don't remember what they
22 thought, they may very well have taught the
23 standard approach; is that fair?

24 A It is.

25 Q You also testified at your

1 deposition that you're not familiar with what an
2 authoritative text is. Do you recall that?

3 A Yes.

4 Q And you couldn't name any particular
5 authoritative text on depreciation. Do you
6 remember that?

7 A Yes.

8 Q Mr. Adam agreed that Depreciation
9 Systems by Frank Wolf and Chet Fitch is an
10 authoritative text when he testified at the
11 hearings in this case, did he not?

12 A Yes.

13 Q In fact, you've also cited the Wolf
14 and Fitch text in sworn testimony that you filed
15 with this Commission, have you not?

16 A Yes.

17 Q And you wouldn't cite in sworn
18 testimony a text unless it was authoritative,
19 would you?

20 A I -- as I said before, there would
21 be some things that I would not fully agree with
22 Mr. Adam on, but the conclusion -- so I would say
23 that I don't -- I find that to be a text on
24 depreciation.

25 Q You wouldn't cite this Commission to

1 a text on depreciation unless you thought that
2 text was authoritative or provided accurate
3 information, would you?

4 A I would cite it as informative.

5 Q But you wouldn't cite it if you
6 thought the information it was providing was
7 inaccurate and that the Commission was thereby
8 going to receive inaccurate information, would
9 you?

10 A Well, I have the NARUC in front of
11 me that I may not agree with.

12 Q That's not the question I asked you,
13 though. The question is whether you would cite a
14 text, in this case the Wolf and Fitch text, to the
15 Commission and provide them information if you
16 didn't believe that text was accurate.

17 A Okay.

18 Q You wouldn't do that, would you?

19 A I believe I have in the past, so if
20 that's a -- something that I'm saying, then yes.

21 MR. LOWERY: Fair enough. May I
22 approach the witness, Your Honor?

23 JUDGE DIPPELL: Yes.

24 COMMISSIONER DAVIS: Could you let
25 us know from what page in Wolf and Fitch you'll be

1 reading from?

2 MR. LOWERY: Absolutely,
3 Commissioner Davis.

4 Q (BY MR. LOWERY) Okay. You
5 recognize this text, do you not?

6 A Yes, I do.

7 Q Could you read the sentence starting
8 with though each.

9 MR. LOWERY: And, Commissioner
10 Davis, I guess you're the only one following along
11 at this point, but I'm on little Roman viii,
12 second paragraph, in the preface, little Roman
13 viii, second paragraph, sentence starting though.

14 Q (BY MR. LOWERY) Would you read that
15 sentence and the next please?

16 A Though each unit in the group has a
17 unique life and salvage, it is the group that is
18 depreciated. This requires the life and salvage
19 of the group be described in statistical terms.

20 Q And read one more sentence, please?

21 A Consequently, analysis of life and
22 salvage data and estimation of future values of
23 life and salvage are a major portion of a
24 depreciation study.

25 Q Thank you. Wolf and Fitch

1 recognizes that estimation of future values of
2 life and salvage are a major portion of a
3 depreciation study. Correct?

4 A He does, and that's where we
5 sometimes get into trouble in our state for -- we
6 cannot do future for additions in electric plant.
7 So, again, when we have a text, if we take it out
8 of context and try to apply it to what we have,
9 that we need to work with, it -- it isn't always
10 applicable.

11 Q When you cited the Wolf and Fitch
12 text in your other testimony, did you take a
13 particular small passage and provide only that
14 small passage in your testimony?

15 A If it was applicable.

16 Q But you did take just a particular
17 passage, correct?

18 A Yes.

19 Q Let me ask you if you agree with
20 another statement. Would you please read the --
21 well, we lost Commissioner Davis. Would you
22 please read the second paragraph on page 51?

23 A The original cost less net salvage
24 is called the depreciable base. It represents the
25 capital consumed during the life of the unit and

1 the amount to be recovered through depreciation.
2 If the net salvage is positive, then the capital
3 consumed is less than the original cost. If the
4 net salvage is negative, the capital consumed is
5 greater than the original cost.

6 Q Do you agree with that paragraph?

7 A Can I look at it again?

8 Q Oh, I'm sorry, sure. Absolutely.

9 A Okay.

10 Q Do you agree with that paragraph?

11 A Can you read that again?

12 Q Sure.

13 MR. LOWERY: Commissioner Davis, if
14 you'd like to follow along, I'm on page 51, second
15 paragraph.

16 COMMISSIONER DAVIS: I'm right
17 there.

18 Q (BY MR. LOWERY) Wolf and Fitch,
19 page 51, second paragraph states, the original
20 cost less net salvage is called the depreciable
21 base. Are we okay so far? Do you agree with that
22 so far?

23 A That's what he says.

24 Q It represents the capital consumed
25 during the life of the unit and the amount to be

1 recovered through depreciation. If the net
2 salvage is positive, then the capital consumed is
3 less than the original cost. If the net salvage
4 is negative, the capital consumed is greater than
5 the original cost.

6 Is it fair to say that Wolf and
7 Fitch indicate they say that part of the capital
8 consumed over time as customers use assets
9 includes negative net salvage?

10 A That's his view.

11 Q Certainly is what Wolf and Fitch
12 says, isn't it?

13 A Yes.

14 Q Do you know Bob White? Do you know
15 who that is?

16 A I could be wrong, but I believe I've
17 met him once.

18 Q Who is he?

19 A Other than what I just told you, I
20 cannot tell you.

21 Q Do you know who Ron White is?

22 A I do.

23 Q He's one of the depreciation experts
24 who provided testimony in this case, is he not?

25 A He was.

1 Q Or he was. How about Harold
2 Wattington [phonetic]?

3 A I do not know him.

4 MR. LOWERY: One more time, Your
5 Honor, and I'll quit approaching her with this
6 book.

7 JUDGE DIPPELL: Go ahead.

8 Q (BY MR. LOWERY) Would you please
9 just familiarize yourself with the second and
10 third full paragraphs on paragraph Roman xi of the
11 preface?

12 A Okay.

13 Q Have you had sufficient time to do
14 that?

15 A How far do you want me to read?

16 Q All the way to the end of that
17 paragraph, the next to last paragraph. Okay.

18 A Okay.

19 Q Thank you. All of the gentlemen
20 that I just mentioned helped Wolf and Fitch in the
21 editing or preparation of this text, did they not?

22 A That's what it says.

23 Q So did Bill Stout, correct?

24 A Yes.

25 Q And those individuals are the

1 individuals that Mr. Stout cited his testimony as
2 being authoritative experts on this subject, are
3 they not? Do you recall that?

4 A I believe so.

5 Q We already talked about the fact
6 that you're familiar with the uniform system of
7 accounts. Correct?

8 A Yes.

9 Q And you testified -- well, let me
10 back up. Uniform system of accounts has been
11 adopted in Missouri. Correct?

12 A Yes.

13 Q And you testify in your supplemental
14 rebuttal testimony that the USOA, I'll use that
15 for short, does not require that the standard
16 approach be used to calculate the net salvage
17 component. Is that your testimony?

18 A Yes.

19 Q We've talked about this a little
20 before, but let's look at that contention a little
21 more deeply. Under the uniform system of
22 accounts, depreciation is defined as follows,
23 quote, depreciation as applied to depreciable gas
24 plant means the loss in service value not restored
25 by current maintenance. That sound right? Sounds

1 correct?

2 A That's fine.

3 Q Clearly the USOA defines
4 depreciation in reference to the service value of
5 the plant, does it not?

6 A Yes.

7 Q And we already established that
8 NARUC's publication does as well, correct?

9 A Yes.

10 Q You don't include the service value
11 concept when you personally define depreciation,
12 do you?

13 A No.

14 Q You leave out the loss in service
15 value concept when you define it. Correct?

16 A Maybe I can clarify how I have it.
17 So that I know what I'm -- I feel like the reserve
18 -- a depreciation reserve, and this is -- this is
19 coming in this state, it is General Order No. 13,
20 it was effective in 1915, a reasonable reserve for
21 depreciation should be set up at the end of each
22 fiscal period sufficient to cover such wear and
23 tear and obsolescence and inadequacy as have
24 occurred during the year in the tangible capital
25 and such portion of the life of the tangible fixed

1 capital as has expired or been consumed during the
2 year. It is not -- it is not required that the
3 salvage be accounted for.

4 Q I understand that it's your
5 contention that it's not. But clearly the uniform
6 system of accounts defines it in reference to
7 service value, and service value clearly takes
8 into account salvage. Does it not?

9 A Yes.

10 Q And when you define in your
11 testimony before this Commission, despite what the
12 uniform system of accounts say, when you provide a
13 definition -- and I'll just read you one. In Case
14 No. ER-2004-0034, in your direct testimony that
15 you filed on December 16, 2003, a few months ago,
16 or I guess several months ago now, you were asked,
17 quote, what is the definition of depreciation?

18 Answer: Depreciation is the loss
19 not restored by current maintenance which is due
20 to all factors, et cetera.

21 And you left the service value
22 concept out of that definition. Correct? That's
23 my simple question.

24 A Yes.

25 Q So when you define depreciation, you

1 typically depart from the definition in the
2 uniform system of accounts and the definition in
3 the NARUC publication. Correct?

4 A Yes.

5 Q If the uniform system of accounts
6 definition is followed, if it is followed, it is
7 true, is it not, that the service value of the
8 asset means the difference between the original
9 cost of that asset and the net salvage value to
10 that asset?

11 A Yes.

12 Q So at least under the uniform system
13 of account, service value's clearly relevant to
14 depreciation and, in turn, net salvage is a part
15 of figuring out what that service value is going
16 to be under the uniform system of accounts, is it
17 not?

18 A Yes.

19 Q I'd like you to make the following
20 assumptions. Assume a utility has a fleet of
21 service trucks and that the average service life
22 on those trucks is ten years. Assume further that
23 experience has shown that on average the utility
24 has historically been able to sell those trucks
25 for 10 percent of their original cost. Twenty

1 thousand truck, 2,000 for it at the end of ten
2 years.

3 Now, in that case, we would have a
4 service value expressed in percentage terms that's
5 positive, 10 percent positive. Correct?

6 A Yes.

7 Q Would it be appropriate for the
8 utility to recover 100 percent of the cost of
9 those trucks in depreciation over that ten year
10 service life?

11 A As me the question again.

12 Q We've got trucks, we've got --

13 A I understand what we have. The
14 question.

15 Q Would it be appropriate for the
16 utility to recover 100 percent of the original
17 cost of those trucks in depreciation over their
18 ten year service life?

19 A They should recover 100 percent.

20 Q So if the truck cost \$20,000 and it
21 has 2,000 of positive net salvage, should they
22 recover \$20,000 in depreciation? Or should they
23 recover 18,000 because you've got to offset that
24 with the positive net salvage?

25 A In the -- if I'm not including in

1 that salvage percentage any depreciation rate,
2 then I would cover only the original cost, and the
3 effect of that salvage would be picked up by the
4 auditors in expense.

5 Q But that's not my question, though.
6 My question is, should the utility recover \$20,000
7 in depreciation --

8 A They would net it. They would net
9 the salvage --

10 Q They should only recover \$18,000,
11 shouldn't they?

12 A Yes.

13 Q And there's not a \$2,000 expense
14 involved, because it's \$2,000 positive net salvage
15 at the end, right?

16 A Yes.

17 Q So the auditors aren't going to pick
18 up a \$2,000 expense, are they?

19 A They're going to pick up the
20 opposite. They'll have the salvage.

21 Q That's right. That's right. But
22 you wouldn't support the utility recovering
23 \$20,000 in depreciation. Correct?

24 A Through the depreciation, I would go
25 ahead and do the full original cost, and then

1 salvage would be picked up by the auditors.

2 Q You would depreciate -- in
3 depreciation you would depreciate 90 percent of
4 the cost of that truck, right?

5 A In the way --

6 Q That's not a trick question.

7 A No. I need to know if I'm including
8 a salvage in the depreciation rate as in the
9 99-315 case or if I'm not.

10 Q Let's assume we are.

11 A Then I would adjust for it.

12 Q Which means you'd depreciate
13 \$18,000?

14 A That is correct.

15 Q Assume now that the law changes or
16 the market changes or some other factor comes into
17 play regarding the trucks, and instead of being
18 able to sell the trucks for 10 percent of their
19 original cost, the utility has to pay somebody to
20 dispose of them at a cost equal to 10 percent of
21 the original cost. Negative net salvage of
22 negative 10 percent in that example. Right?

23 A Yes.

24 Q So the service value of the trucks
25 is no longer 90 percent, it's now 110 percent.

1 Right? Assume we're dealing with it in the
2 depreciation.

3 A That's correct.

4 Q Isn't it fair to say that, you're
5 going to be consistent, you have to depreciate 110
6 percent of that over the service life; otherwise,
7 you're not ratably allocating the entire service
8 value of the trucks over their life, are you?

9 A For that unit, that would be
10 correct.

11 Q You agreed in your deposition that
12 the uniform system of accounts requires accrual
13 accounting, correct?

14 A That's what it states.

15 Q That it requires it. Correct?

16 A Yes.

17 Q And you also agreed that your
18 approach, the -- is it okay if I call it the
19 expensing approach? Cash approach?

20 A We have two different concepts.
21 Whichever one you want me to --

22 Q Your approach. The one that you
23 personally typically recommend.

24 A Okay.

25 Q You agree that your approach is not

1 accrual accounting, right?

2 A That is correct.

3 Q And we earlier agreed that Mr.
4 Adam's approach and your approach produce
5 substantially equivalent results. And Mr.
6 Oligschlaeger testified that they are
7 substantially the same, did he not?

8 A Correct.

9 Q If Mr. Adam's approach and the
10 expensing approach, your approach, the one you
11 typically recommend, produce substantially
12 equivalent results, then Mr. Adam's approach can't
13 very well be accrual accounting, can it?

14 A I will refer that to Mark
15 Oligschlaeger.

16 Q Well, you gave an opinion before, I
17 believe, in your deposition about your approach
18 not being accrual accounting. You're just not in
19 a position to give an opinion about --

20 A I think it's better --

21 MR. SCHWARZ: Object, the question
22 has been asked and answered, and the witness has
23 indicated it's best addressed to another witness.

24 JUDGE DIPPELL: She didn't actually
25 answer the question, though. She just said she

1 would defer that -- I don't believe that the
2 question that was asked was asked of Mr.
3 Oligschlaeger, it was asked of Miss Schad. You
4 may ask.

5 Q (BY MR. LOWERY) Put it this way.
6 You're unwilling to concede, as you sit here
7 today, even though both approaches produce
8 substantially equivalent results and you have
9 conceded that your approach is not accrual
10 accounting, you're not willing to concede that Mr.
11 Adam's approach is not accrual accounting. Is
12 that fair?

13 A In the sense that I feel it is
14 accruing for it.

15 Q Well, if they produce substantially
16 equivalent results and one is not accrual
17 accounting, then regardless of the label we put on
18 it, the effect of Mr. Adam's approach is the same
19 as the effect of your approach which is not
20 accrual accounting; do you agree with that?

21 A I would agree with that.

22 Q You've cited a 1990 MoPub case as a
23 case where the Staff recommended an approach that
24 was similar to the approach Mr. Adam took in this
25 case; right?

1 A That is correct.

2 Q And you said at your deposition that
3 Mr. Adam's approach does not contain a factor that
4 addresses inflation in the way Mr. Love addressed
5 that factor in the 1990 MoPub case; is that
6 correct?

7 A That is correct.

8 Q And also a subsequent 1993 MoPub
9 case, right?

10 A Yes.

11 Q And you refer us to those cases
12 because you contend that they show that Staff has
13 been taking Mr. Adam's approach, or something akin
14 to it, even though his doesn't address inflation
15 in any way, for a while; is that fair? Is that
16 the point you're making in citing the 1990 and
17 1993 cases?

18 A I'm making the point that Staff has
19 taken an issue that evolves over time, and it has
20 evolved and has evolved a lot in the last 80
21 years, and still try to retain the same
22 understanding of it and try to attempt to achieve
23 the same goals. And with -- in that evolvment,
24 there have been offshoots.

25 But my -- my position in referencing

1 those is because with mass asset accounts, which
2 is very important to understand we're not talking
3 about life span plan here which has the event way
4 into the future, we're not trying to take mass
5 asset accounts way into the future either. We're
6 trying to provide the customers in the rate case a
7 level of cost for those costs if they are going to
8 incur while they are subject to those rates.

9 Q What's the average service life in
10 Laclede's gas main account in this case used by
11 Mr. Adam?

12 A I would have to look at that.

13 Q If I told you it was 84 years, 85
14 years, does that sound about right?

15 A I know when I did the analysis, it
16 was less than that. I know my number. I'd have
17 to look at his.

18 Q Well, we can certainly do that. Do
19 you have Exhibit 124 in this case? And I've got
20 it here.

21 MR. LOWERY: May I approach, Your
22 Honor?

23 JUDGE DIPPELL: Yes, that's fine.
24 Mr. Lowery, do you still have substantial
25 questions for this witness?

1 MR. LOWERY: Enough that you may
2 want to have lunch, yes.

3 JUDGE DIPPELL: Okay. Why don't we
4 go ahead and take this lunch break, and we will
5 break for just an hour and four minutes, we will
6 come back at 1:35. And begin again -- and at that
7 time we will probably go ahead and finish with
8 Miss Schad, and then after she's finished, we will
9 call back Mr. Lyons and Mr. Sherwin for Commission
10 questions, unless those parties are -- Mr. Byrne
11 looks like he's --

12 MR. BYRNE: No, thank you, they
13 appreciate being called back as soon as you can.

14 JUDGE DIPPELL: They don't have any
15 conflicts this afternoon with airline tickets or
16 --

17 MR. BYRNE: No, Your Honor.

18 JUDGE DIPPELL: All right, then.
19 Let's go ahead and break for lunch and come back
20 at 1:35. We're off the record.

21 (Off the record.)

22 JUDGE DIPPELL: Okay, we're back on
23 record. And Miss Schad has returned to the
24 witness stand. You may continue with your cross
25 examination, Mr. Lowery.

1 Q (BY MR. LOWERY) Good afternoon.

2 A Good afternoon.

3 Q I think right before we left, we
4 were talking about the 1990 and 1993 MoPub cases
5 that you had referred us to in some of your
6 testimony, correct?

7 A Yes.

8 Q Did you make mention of Staff's
9 treatment in Case No. ER-97-394?

10 A I think I made mention of the order
11 itself.

12 Q That's correct. You didn't make
13 mention of how the net salvage percentages were
14 calculated in that case, did you?

15 A I don't believe so.

16 Q That was also a MoPub case, was it
17 not?

18 A Yes, it was.

19 MR. LOWERY: May I approach the
20 witness?

21 JUDGE DIPPELL: Yes.

22 Q (BY MR. LOWERY) Miss Schad, I've
23 just handed you a copy of Guy Gilbert's direct
24 testimony from 97-394, and I apologize for the
25 quality of the copy, but that's as good as the

1 microfilm machine downstairs will do.

2 A Okay.

3 Q Have you read this testimony?

4 Recently?

5 A No.

6 Q Can I direct your attention to page
7 4, starting on line 5?

8 A Can I rephrase? I did try to
9 recapture what Mr. Stout had in his testimony, and
10 to refer back to that --

11 JUDGE DIPPELL: Miss Schad, I'm
12 going to need you to speak up. We can't hardly
13 hear you up here.

14 THE WITNESS: Okay. I have read a
15 portion of it lately.

16 Q (BY MR. LOWERY) Okay. Fair enough.
17 Can I ask you to read starting on page 4, line 5,
18 through page 5, line 8?

19 MS. O'NEILL: Your Honor, at this
20 time I'm going to object, relevance. This is a
21 Laclede Gas rate case from 1999. Mr. Gilbert is
22 not a witness in this case, I just don't see that
23 we're getting anywhere with this. I don't see how
24 it's relevant, and I think it's basically unduly
25 complicating this entire matter. It's redundant,

1 and I would ask that Counsel move on.

2 MR. LOWERY: May I respond?

3 JUDGE DIPPELL: Yes, please.

4 MR. LOWERY: Your Honor, Mr.

5 Gilbert's testimony will reflect that he used this
6 standard approach in 1997. Miss Schad has
7 directed us to cases in 1990 and 1993 involving
8 the same utility in support for the contention
9 that Staff has been using Staff's approach since
10 1990. This is clearly admission of a party
11 opponent, consistent with that contention, it's
12 clearly relevant on that issue.

13 MS. O'NEILL: Can we do that without
14 reading two pages of testimony into the record?

15 JUDGE DIPPELL: Okay, I'm going to
16 overrule your objection. Proceed, Mr. Lowery.

17 Q (BY MR. LOWERY) Do you -- do you
18 remember the pages and line numbers that I asked
19 you to read?

20 A Would you repeat those?

21 Q Sure. Page 4, starting at line 5,
22 to page 5, line 8.

23 A Okay. So I'm going to be page 4,
24 line 4?

25 Q Starting at page 5, the question

1 **that starts, are there any overriding differences.**

2 A Oh, okay. Are there any overriding
3 differences in the methods and assumptions used in
4 your depreciation study from those used in
5 previous Staff studies for this company?

6 Yes, the single largest difference
7 is that interim net salvage has a greater cost of
8 removal component than was previously recognized.
9 This results from the method and assumptions used
10 in determining the net salvage estimates.

11 Explain how you arrived at your net
12 salvage estimates.

13 Net salvage used in determining a
14 depreciation rate comprises two components as
15 follows. Gross salvage, which is received through
16 sale of scrap material, equipment, parts returned
17 to stock, or other sources; and cost of removal
18 required to retire, dismantle, and remove from
19 service and dispose of retired property. I'm
20 sorry, retired plant.

21 Net salvage equals gross salvage
22 less cost of removal and most generally is
23 negative for most accounts, that is cost of
24 removal is greater than gross salvage.
25 I analyzed past retirements and net salvage

1 dollars recorded on the books of the utility and
2 computed the percentage of net salvage by
3 calculating the ratio of the net salvage dollars
4 to dollars retired.

5 I used these percentages in the
6 calculation rates which are applied to the
7 surviving plant investment contained on the
8 company's books.

9 I'm sorry, which line did you want
10 me to --

11 Q Just so we don't talk about data
12 files, I'll try to save a little bit, just skip
13 over to the next page and read lines 4 to 8.

14 A How had Staff previously determined
15 the net salvage percentage?

16 Previously in Case No. ER-93-37,
17 Staff had calculated the ratio of net salvage
18 dollars to total plant in service dollars by
19 account to derive a percentage of net salvage for
20 inclusion in a depreciation rate calculation.
21 This did not reflect net salvage properly as the
22 ratio of net salvage to the book value of plant
23 retired.

24 Q Mr. Gilbert is describing, in that
25 testimony, that he was using the standard approach

1 to calculating the net salvage percent, was he
2 not?

3 A Yes, he was.

4 Q And that's in contrast to what Mr.
5 Love did in 1990 and 1993 with respect to the same
6 utility, correct?

7 A Yes.

8 Q And you testified in your deposition
9 that you didn't know how Staff was treating net
10 salvage for Laclede or for UE or for MoPub or any
11 other electric or gas utility, for that matter,
12 prior to the 1990 MoPub case, right?

13 A That's correct.

14 Q And you also testified at your
15 deposition that you don't know how Staff treated
16 net salvage for mass property accounts in other
17 cases between 1990 and 1999; is that correct?

18 A That is correct.

19 Q Witnesses for Laclede and Ameren UE
20 have testified that for decades the standard
21 approach was used for their companies, have they
22 not?

23 A That is correct.

24 Q You agreed at your deposition that
25 Laclede's distribution system was substantially

1 smaller in terms of number of cust --

2 MS. O'NEILL: Your Honor, if I can
3 interject in the interest of time, again, it's my
4 understanding that the parties have all agreed
5 that depositions may be entered into the record as
6 evidence.

7 I don't see any reason for us to go
8 through question and answer by question and answer
9 from Ms. Schad's deposition if that's going to be
10 part of the record in that case. So I would
11 object, duplicative.

12 MR. LOWERY: Your Honor, I have just
13 probably ten or 15 minutes of cross left at most.
14 Some of the questions will refer to the
15 deposition, some of them won't. I think it's
16 appropriate to highlight for the Commissioners
17 that are here the most relevant parts of the
18 deposition from our perspective.

19 JUDGE DIPPELL: I'm going to allow
20 it just so that we can make clear when the -- Mr.
21 Lowery is referring to portions of the
22 depositions. The depositions of -- the parties
23 did indicate to me that they have decided -- have
24 agreed to admit those, have not yet been admitted
25 into the record, so we're just going to go ahead

1 and let Mr. Lowery ask his questions.

2 MR. LOWERY: I apologize, can you
3 read back at least the beginning of the last
4 question so I can see where I was? Not sure what
5 I asked her.

6 THE WITNESS: I believe the last
7 sentence was, this did not reflect net salvage
8 powerfully as the ratio of net salvage to the book
9 value of plant retired.

10 MR. LOWERY: I'm sorry, I was asking
11 the court reporter. I apologize.

12 THE REPORTER: "You agreed at your
13 deposition that Laclede's distribution system was
14 substantially smaller in terms of number of --"

15 Q (BY MR. LOWERY) Miles of pipe, et
16 cetera, in the 1920s and the 1930s than it is now.
17 Correct?

18 A Yes.

19 Q You also agreed one of Laclede's
20 largest accounts is gas mains?

21 A Yes.

22 Q And cast iron gas mains, average
23 service life is around 70 years, correct?

24 A Yes.

25 Q You also agree that if there's

1 nothing unusual going on like road construction,
2 all other things being equal, cast iron gas mains
3 removed in the 1990s, would have been put in
4 service around 70 years prior on average, correct?

5 A Can you ask that question again?

6 Q Can you also agree, did you not,
7 that if there was nothing unusual going on like
8 road construction that might require newer gas
9 mains to be removed, all other things being equal,
10 cast iron gas mains removed in the late 1990s, in
11 other words, in the few years preceding this case,
12 would have been put in service around 70 years
13 before on average. Correct?

14 A Yes.

15 Q And you testified, did you not, that
16 Laclede's system was a lot smaller back then?

17 A Yes.

18 Q And there's been substantial
19 customer growth for Laclede since the '20s and
20 '30s, has there not?

21 A Yes.

22 Q You also testified that you don't
23 include a factor in your calculation of net
24 salvage to account for the fact that there's been
25 customer growth of that type. Correct?

1 A That's correct.

2 Q I believe you agree that
3 intergenerational equity means that each
4 generation of customers should pay the full cost
5 the utility incurs to provide them service. Is
6 that fair?

7 A For equity, yes.

8 Q And you also agree, as a general
9 principle, that it's unfair for past or future
10 generations of customers to subsidize today's
11 customers?

12 A Yes.

13 Q And you agree that the Commission
14 ought to consider that sort of intergenerational
15 equity, those kinds of issues, when it sets rates?

16 A Yes.

17 Q On page 12, lines 19 to 20 of your
18 supplemental rebuttal testimony, you state that
19 current customers are realizing continued service
20 due to retiring and removing plant for which there
21 was a cost of removal expense. Did I state that
22 accurately?

23 A I think so.

24 Q In order for those customers to
25 realize that continued service, not only does the

1 utility have to remove the old plant, let's say an
2 old service line, but the utility also has to put
3 in the new service line, does it not?

4 A It does.

5 Q So you have to also recognize that
6 current customers are recognizing current service
7 due to the installation of the new line; correct?

8 A Yes.

9 Q Are you suggesting that because they
10 are realizing service due to the installation of
11 the new line that we should follow the same
12 approach and expense the new line instead of
13 capitalizing it?

14 A No, I am not.

15 Q Well, for Laclede, if we took -- if
16 we took the -- it allows continued service
17 approach and, thus, we did expense that new line
18 because it allows continued service, right? That
19 new line allows continued service, correct?

20 A That is correct.

21 Q Let's say we did that for Laclede.
22 Laclede's annual revenue requirement would
23 increase from around 20 million per year to around
24 50 million per year related to this issue,
25 wouldn't it?

1 A I would assume so.

2 Q But you wouldn't support that even
3 though the new line is also essential to continued
4 service, is that your testimony?

5 A That is correct.

6 Q You testified in your deposition
7 that a generation that is incurring a loss is a
8 generation that's paying for the loss is what I
9 would call intergenerational equity. Do you
10 remember that?

11 A Yes.

12 Q The level of expense allowed under
13 your method are derived from past cost for removal
14 of plant that is now out of service. Correct?

15 A I believe as you said that, that
16 would be, yes.

17 Q And that plant was installed many
18 years ago to serve customers who were around when
19 it was installed, to serve those customers who
20 were there when it was installed, and to serve
21 customers that existed until the day it was
22 retired. Correct?

23 A Correct.

24 Q And it is the generation of
25 customers who needed service back when the plant

1 was installed that caused it to be installed.

2 Correct?

3 A Yes.

4 Q And if the plant had not been
5 installed in the first place, it obviously could
6 not later be retired.

7 A That is correct.

8 Q And the generation or probably
9 generations of customers who were served by the
10 plant were the generations who used it from the
11 time it was installed until it was retired.
12 Right?

13 A That is correct.

14 Q Those generations should pay the
15 costs associated with that plant that they use,
16 shouldn't they?

17 A They should.

18 Q You also testified at your
19 deposition that in general you support the
20 matching principle, do you not?

21 A Yes.

22 Q And you agree that the idea behind
23 the matching principle is that a utility's revenue
24 should be matched to its costs so the customers
25 pay rates that reflect the cost incurred to

1 provide them service. Right?

2 A Can you repeat that?

3 Q Sure. You agree, I think, that the
4 idea behind the matching principle is that a
5 utility's revenue should be matched to its cost so
6 that the customers pay rates that reflect the cost
7 incurred to provide those customers service.

8 A Yes, I do, and I also, in that
9 context, have demonstrated that what the standard
10 approach there is trying to do is attempt to place
11 some future estimated unknown cost onto these rate
12 payers. On the generation of rate payers.

13 Q The future costs that are estimated
14 under the standard approach are costs associated
15 with removing plant that is currently in service,
16 correct?

17 A It is; however, we don't know that
18 they will occur the predictive nature of that --
19 of the standard ratio, as you defined it earlier,
20 does not predict that future cost, and that is
21 what the Staff's concern is with it. It is not
22 predictive -- it is not a predictive measure.

23 Q In your opinion, it's not a
24 sufficiently accurate predictive measure, but the
25 goal of the standard approach is to predict those

1 costs, is it not?

2 A I have not seen by any expert to
3 date a study that shows it's predictive, and that
4 is -- and I have not -- well, perhaps, perhaps a
5 demonstration. I should do a map. I would like
6 to --

7 Q That's fine. That's fine. We'll
8 move on. Do you agree that when plant is
9 abandoned, let's say a gas plant, gas main,
10 service line, when plant's abandoned, there are
11 often costs associated with its abandonment,
12 digging down, cap the line, purge the line, those
13 types of things?

14 A Yes.

15 Q So even if a property is abandoned
16 in place, there may be negative net salvage
17 associated with it, correct?

18 A There could be costs of removal,
19 yes.

20 Q And those costs of removal may very
21 well exceed any salvage that you could obtain for
22 that pipe, for example. Correct?

23 A Yes.

24 Q Are you suggesting that gas
25 utilities who decide to abandon a pipe in place

1 should not dig down, isolate that pipe from the
2 system, purge it, bury it again, repave over it if
3 that's necessary; is that your suggestion in some
4 of your testimony where you talk about we don't
5 know if those costs are going to be incurred?

6 A When I say I don't know if costs are
7 going to be incurred, I mean I do not know if in
8 the future a cost will be incurred.

9 Q We know in the past that costs have
10 been incurred, don't we?

11 A Costs have been incurred in the
12 past.

13 Q Isn't it true that the net salvage
14 ratio and the net salvage percent ratio used in
15 the standard approach takes into account that some
16 plant is actually dug up and completely removed
17 and some plant is abandoned in place?

18 A It takes into account that there's
19 costs incurred.

20 Q And it takes into account --

21 A I would think that there's both of
22 those inclusive in that.

23 Q There are, in the data used to
24 calculate that ratio, there are -- there is data
25 that represents plant that was completely removed

1 at perhaps a higher cost and plant that was
2 abandoned in place at some cost, but perhaps lower
3 than the -- lower than removing it entirely.

4 Correct?

5 A Yes.

6 Q So the analysis employed in the
7 standard approach does reflect a historical mix of
8 removal versus abandonments; is that fair?

9 A Yes.

10 Q And you agreed at your deposition,
11 did you not, that for mass property, we actually
12 do have data involving Laclede showing actual
13 retirements and removals in the past, correct?

14 A Yes.

15 Q On page 13, lines 11 to 16 I believe
16 of your supplemental rebuttal testimony, you cite
17 a passage from the ER-97-394 case and that passage
18 dealt with terminal net salvage costs, did it not?

19 A I believe so.

20 Q I think you testified earlier today
21 in answer to some of my other questions, you were,
22 in fact, I think emphatic that this case does not
23 involve terminal net salvage. Correct?

24 A That is correct.

25 Q It's a mass property case, right?

1 A Yes.

2 Q This Commission has never made the
3 statements that you quote from that ER-97-394 case
4 with regard to mass property, has it?

5 A With regard to being known and
6 measurable?

7 Q The quote that you cited dealt with
8 terminal net sal --

9 A Yes, it did.

10 Q Did it refer to the issue of whether
11 terminal net salvage costs are known and
12 measurable, correct?

13 A Correct.

14 Q You haven't cited us to any
15 Commission decision that makes those same
16 statements with respect to mass property, have
17 you?

18 A There may be something in a later
19 case, if I can have a moment to look through it.

20 Q Well, if there were, why didn't you
21 cite it in your testimony, since you were so
22 emphatic that this is a mass property case?

23 MR. SCHWARZ: I'll object to the
24 form of the question as argumentative.

25 MR. LOWERY: I'll withdraw the

1 question.

2 JUDGE DIPPELL: Okay. That works.

3 THE WITNESS: I was ready to answer.

4 Okay.

5 MR. LOWERY: I'll withdraw the

6 question.

7 Q (BY MR. LOWERY) On page 14, line 3
8 to 6 of your supplemental rebuttal testimony, you
9 suggest that Mr. Fetter's reference to a recent
10 Indiana Public Utility Commission decision that
11 endorses the standard approach related to
12 generating plants. Is that the point you were
13 making?

14 A Yes.

15 Q You're wrong about the quote that
16 Mr. Fetter cites on that page of his testimony,
17 aren't you?

18 MR. LOWERY: May I approach the
19 witness, Your Honor?

20 JUDGE DIPPELL: Yes. You want to
21 show that to Counsel?

22 MR. LOWERY: Sure. She references
23 the quote on page 8 of Mr. Fetter's testimony,
24 which is right here.

25 Q (BY MR. LOWERY) I'll just give you

1 an opportunity to read the quote that you
2 referenced in your testimony. Tell me when you've
3 finished reading that, please.

4 Don't mean to rush you, but have you
5 had a chance to read the quote on page 8?

6 A No.

7 Q Sorry.

8 A Okay.

9 Q Thank you. The Indiana Commission
10 was talking about transmission and distribution in
11 general plant, were they not?

12 A Can you --

13 Q Accordingly -- let me ask you if I
14 am reading this accurately. Accordingly, we find
15 that the use of historical averages for net
16 salvage values with regard to transmission,
17 distribution, and general plant for the purpose of
18 expensing them outside the context of the
19 depreciation determination should be and hereby is
20 rejected. Do you recall reading that?

21 A Yes.

22 Q And that's what you do in the method
23 that you typically recommend is you expense them
24 outside of depreciation, do you not?

25 A Yes.

1 Q And they were not referring to
2 generation plant, correct? Transmission,
3 distribution, and general plant is not generation
4 plant. It's not life span property, correct?

5 A No, it's not.

6 Q And we've already agreed that
7 Laclede has had retirements of mass property on a
8 regular basis in the past. Correct?

9 A Yes.

10 MR. LOWERY: Thank you.

11 JUDGE DIPPELL: Is there cross
12 examination from Laclede?

13 MR. ZUCKER: Yes, Your Honor.

14 JUDGE DIPPELL: Okay. Before -- I'm
15 sorry, Mr. Zucker, Commissioner Appling has to
16 leave and he was going to -- he has some questions
17 of this witness. So I'm going to interrupt for a
18 moment --

19 MR. ZUCKER: I will be glad to
20 defer.

21 JUDGE DIPPELL: -- and I'll let him
22 ask his questions.

23 BY COMMISSIONER APPLING:

24 Q Good afternoon.

25 A Good afternoon.

1 Q Just a couple questions, hopefully I
2 can clear up a point for me before I depart. This
3 morning Mr. Stout testified that he -- to his
4 knowledge, the first use of the cash method for
5 net salvage occurred in Pennsylvania in 1962. Do
6 you agree with that statement?

7 A I -- I know it's -- was utilized in
8 Pennsylvania. I don't know the year.

9 Q The year, or whatever case is.
10 Okay. He also said that its use was limited in
11 Pennsylvania until 1990 when Missouri PSC Staff
12 proposed cash method for net salvage in several
13 rate cases. Do you agree with that?

14 A Well, there was a time in Missouri,
15 but it's -- that's far back, because at one time
16 there was a time when the uniform system of
17 accounts expensed cost of removal, but it was
18 earlier in the decade.

19 Q Mm-hmm. Okay. In your opinion,
20 what led Staff to propose the cash method when the
21 accrual method had been used for so long?

22 A Can I actually demonstrate that on
23 -- I mean, it's easier for me to do it with some
24 numbers.

25 Q I want it cleared up for me, so if

1 **you want to demonstrate, you can.**

2 JUDGE DIPPELL: Miss Schad, are you
3 going to use that?

4 THE WITNESS: Yes.

5 JUDGE DIPPELL: Would you be willing
6 to attempt to do it electronically if I turn on
7 the smart board behind you? Or are you more
8 comfortable using the --

9 THE WITNESS: I'm not sure if I'm
10 familiar with this.

11 JUDGE DIPPELL: You'd just write on
12 it like you'd write on that. I need to turn it
13 on.

14 THE WITNESS: I can.

15 JUDGE DIPPELL: Mr. Schwarz, could
16 you help me out? There's a power button on that
17 projector? On the underneath side there.

18 **Q (BY COMMISSIONER APPLING) Again, my**
19 **question was what led Staff to --**

20 **A And I want to show you what's in our**
21 **minds and what's happening.**

22 JUDGE DIPPELL: But I will need you
23 to speak up because -- since you're away from the
24 microphone. We'll see how this works. Hang on
25 just a minute. There it goes. Okay. Now, if you

1 write on that, and then if you need to erase, you
2 pick up that round eraser and just erase it.

3 THE WITNESS: Okay. Let's say for
4 an account, okay, this is representative of what
5 has occurred. I'm sorry. This is not -- I have
6 to use this. You'll have to bear with me.

7 JUDGE DIPPELL: I know, I'm excited
8 that we get to use it, but if it doesn't work out,
9 Miss Schad, we'll go back to the other board.

10 THE WITNESS: Okay. So in an
11 account, if I have a cost of removal and I have
12 some salvage and I'm going to determine what's my
13 net cost, or net salvage, you could go either way.
14 And, in fact, it did go -- it was salvage until,
15 you know, probably the '60s. But it has reversed
16 for the moment.

17 So I need to know how much of that
18 account is my -- okay. That is the cost of
19 removal for that account. Okay? And if I was to
20 use, let's say, the standard approach, this cost
21 of removal divided by the dollars it was retired
22 for that year, and I'm going to use one year, so
23 this is a picture of one year.

24 I'm going to, if you would, at
25 December 31, I'm going to look at that past year

1 and have just one year ahead, or I can apply to
2 however many years, but it's just taking one
3 snapshot of a year in time. And I can do two
4 years, five years, I can do a rolling average.

5 And that's a percentage, and it's
6 negative. If, in this account, if the average
7 service life has been shown to be 34 years, and
8 I'm taking -- if -- if one assumes that we must
9 use a certain way to derive depreciation, and in
10 this state that has not been -- it has not been --
11 the Commission has never told us you must use a
12 certain way.

13 So if this is -- that's 100 percent
14 minus the net salvage percent, and you'll see this
15 over and over again, 100 percent minus the net
16 salvage percent. And this is my net salvage
17 percent. And it has to be negative so it ends up
18 being -- ends up adding.

19 So I have my full total original
20 cost which is 100 percent, and now I need to add
21 something that's almost 300 percent in addition.
22 So after I take it out of percentage form, I have
23 this. And now I'm going to apply it to the end of
24 the year plant balance for this account.
25 453,852,242. And that's multiplied times that.

1 What this generates is 37 million
2 dollars. But the actual expenditure for the year
3 is only 3 million. Such charge overaccruals. And
4 this will continue until it's reviewed again. And
5 the significance of this was this is an actual
6 count, these are actual dollars from an Ameren UE
7 364 account. At the end of 1996.

8 What Mr. Adam would have done, what
9 he would have backed into this, and he would have
10 said one minus some percentage over the life of
11 the account needs to equal this number. And when
12 he -- and this is what Mr. Love did in 1990 as
13 well. And that percentage was a negative 0.2253.

14 So what I have occurring here,
15 instead of a 2.78, which would be the standard
16 approach for only one year as defined there, when
17 I do that, I generate such large sums of moneys,
18 such overaccruals, such overcharges to today's
19 customers.

20 Because if in this year -- so if in
21 the year 1997, that customer is paying his O and M
22 expenses that keep the system going, plus there's
23 plant being retired, but being replaced so that
24 his system continues, once he pays this amount and
25 he -- if he's off the system in a year, he has now

1 made the system whole such that it would provide
2 service for 10, 15 years into the future in
3 addition to all the O and M expense that he is
4 paying for that year in order to make the system
5 whole, in order to continue the service. But he
6 pays this not just for himself, but for future
7 customers.

8 Now, the problem came into is that
9 up until the '50s, there was just a -- for a --
10 like a gas account was just 1.5 percent of the --
11 like a bucket of dollars.

12 Q (BY COMMISSIONER APPLING) My next
13 question would be, did you all model this model
14 after Pennsylvania or did you all -- did Mr. Adam
15 and Mr. Love create their own formula here for
16 this? Was this modeled after Pennsylvania's?

17 A No. I think what happened was there
18 was the -- like for any other cost, as in -- as in
19 what has -- for any expense or cost, what that
20 customer -- what customer should be included in
21 the cost of service, a cost increase is known if
22 it is certain to occur, and it is measurable if
23 the Commission is able to determine the amount of
24 the increase with reasonable precision.

25 And that -- this is from the St.

1 Louis County Water Case 2000-844. So the
2 Commission traditionally and properly allows
3 recovery of cost increases that are projected to
4 occur after the end of the test year, including
5 any adjustment periods, only if those costs are
6 known and measurable. But went on to say a cost
7 increase is known if it is certain to occur and it
8 is measurable if the Commission is able to
9 determine the amount of the increase with
10 reasonable precision.

11 And if -- if I take this phenomenon
12 and build it to where a company doesn't come back
13 in for several years, as Ameren UE did from 1983
14 until the complaint case, there was developed a
15 billion dollars overaccrual from this in addition
16 -- between this and a small change of average
17 service lives. It is that kind of concern that
18 has concerned Staff.

19 Q Okay. In the name of time, let me
20 ask you my final question, okay?

21 A Okay.

22 Q In the future, would you recommend
23 using the cash approach in any rate case, or would
24 you only recommend it for special purposes?

25 A Well, I think that there has to be a

1 lot of clarification by the Commission as to what
2 they want depreciation to be. What I read in the
3 1913 -- the 1915 there, the reserve was for the
4 loss in service value. There was no concept even
5 at that point of net salvage, cost of removal.
6 The reserve was specifically for the loss of its
7 service ability.

8 The dilemma that we have gotten into
9 in our state over the years is this has not been
10 defined how it must be derived. This is an
11 estimate. This is an estimate that, as I've
12 pointed out, judgment is used. There's no doubt
13 about it. What we do have in that instance is
14 that engineers in the '30s were able to take
15 industrial property and empirically derive ways to
16 -- to look at data.

17 But the purpose of depreciation has
18 to be defined in our state. If -- if cash flow is
19 going to be a driver, if that's going to be
20 brought into the picture, then we -- we do that.
21 I mean, we will do what we -- we should do. If
22 that's what this Commission should decide.

23 And when you expense it, when you --
24 if -- if fine tuning -- as we saw here, in the '97
25 case, this was done. We don't say we didn't. I

1 really, you know, I looked at it after Mr. Stout
2 put it in his testimony. I took a look at it.
3 It's the fine tuning that's going on. It is what
4 should be the cost.

5 I think I said in my direct
6 testimony, the question here is what is the cost
7 that should be allowed for Laclede. And if -- if
8 the fine tuning means there should be some
9 inflation factor. But by no means has the
10 standard approach been used for decades in our
11 state because there was a flat percentage for --
12 until just about 40 years ago.

13 COMMISSIONER APPLING: Okay. Thank
14 you.

15 JUDGE DIPPELL: Miss Schad, thank
16 you for being our first guinea pig on this. Don't
17 erase anything. Leave it as is. I want to save
18 it. Would you just reach up and touch the little
19 icon at the top that looks like a diskette for
20 save?

21 THE WITNESS: What I wanted to say
22 also, Commissioner Appling, is that in this
23 situation, the order was -- and Mr. Stout brought
24 this up in his supplemental --

25 Q (BY COMMISSIONER APPLING) What I'm

1 trying to get clear in my mind is the two models.
2 Whether you fall into Pennsylvania or whether you
3 create your own. It's not the standard model.
4 That's what I'm trying to get at. Is this a
5 creation of Staff's or is it modeled behind the
6 Pennsylvania model?

7 A It is Staff's. It is Staff's. And
8 I would agree, if we were to look at these trends
9 in the order back in this, this percentage for
10 this was 1.27. I don't agree that we have trends.
11 What the problem is, is those -- it's not
12 predictive. And -- and Staff has -- Staff -- your
13 Commission has been very fortunate to have
14 personnel on Staff over the years, long before I
15 came, that really take a look at what's going on.

16 COMMISSIONER APPLING: Okay. We're
17 going to move on in the name of time, okay? Thank
18 you very much.

19 JUDGE DIPPELL: If you'd just reach
20 up with your finger and touch the little icon up
21 there on the menu that looks like a diskette for
22 save? Yes. That one. That will actually save
23 it. And then you can sit down. Thank you.

24 And I am going to mark that as
25 Exhibit 148 so that it's going to be saved in the

1 record. And that is currently on the C drive of
2 the computer that is at the witness stand, and I
3 will get it printed out so that Counsel can have a
4 copy of it.

5 THE WITNESS: Mr. Appling, can I
6 just say, in Staff's approach, this would be the
7 amount, as cash. That 3 million.

8 COMMISSIONER APPLING: Okay. Thank
9 you very much. It's clear as water. For an old
10 country boy like me.

11 THE WITNESS: I'm sorry. Is it not?
12 Did I not do --

13 COMMISSIONER APPLING: You answered
14 my question.

15 JUDGE DIPPELL: Thank you. Thank
16 you for that little departure there. We'll let
17 Laclede go ahead and come up to ask their
18 questions, then. And, Mr. Zucker, if you want to
19 just do your regular cross and save any recross
20 you have, it might be less confusing, rather than
21 --

22 MR. ZUCKER: Okay. I'd be willing
23 to do that.

24 JUDGE DIPPELL: If that makes it
25 more confusing --

1 MR. ZUCKER: Just for me.

2 JUDGE DIPPELL: Go ahead, but I'm
3 not going to let you have two chances to have
4 questions about Commissioner Appling's questions,
5 that's my point.

6 MR. ZUCKER: In that case, I'll save
7 them.

8 CROSS EXAMINATION BY MR. ZUCKER:

9 Q Good afternoon, Mrs. Schad.

10 A Good afternoon.

11 Q I'm Rick Zucker, I'm an attorney for
12 Laclede Gas Company. Good to see you.

13 A Thank you.

14 Q I don't want to go over too much old
15 ground that Mr. Lowery covered, but just very
16 quickly, would you agree that Mr. William Stout,
17 the President of the valuation and rate division
18 at Gannett Fleming, Inc., is a depreciation
19 expert?

20 A I believe I said earlier that when
21 he testifies in Missouri, that would satisfy that.

22 Q How about when he's not testifying
23 in Missouri?

24 A Outside of the context of what we
25 use as expert here as far as testifying, there --

1 there isn't a -- there isn't a body that has the
2 power to ascribe practices to define what an
3 expert is, the power to sanction any deviating
4 actions in -- in that context.

5 Q Would you consider him an expert?

6 A Yes.

7 Q Would you also agree that he is an
8 expert in net salvage specifically?

9 A He has -- yes.

10 Q Do you have your rebuttal testimony
11 with you?

12 A Yes.

13 Q Could you turn to page 5 of that
14 testimony?

15 A Okay.

16 Q At line 22 there, a question is
17 asked of you in which a -- it is -- Mr. Lyons'
18 view is recited that Staff's approach is
19 inconsistent with the standard regulatory practice
20 recommended by NARUC. Do you see that?

21 A Yes.

22 Q And on page 6, line 7, you respond
23 with a paragraph from page 157 of NARUC's Public
24 Utility Depreciation Practices. Do you see that?

25 A Yes.

1 Q And your response starts with the
2 phrase, some commissions have abandoned the above
3 procedure. You see that?

4 A Yes.

5 Q What is the above procedure? Do you
6 have a Public Utility Depreciation Practices book
7 there?

8 A Historically most regulatory
9 commissions have required that both gross salvage
10 and cost of removal be reflected in depreciation
11 rates. The theory behind this requirement is that
12 since most physical plant placed in service will
13 have some residual value at the time of its
14 retirement, the original cost recovered through
15 depreciation should be reduced by that amount.

16 Q Continue, please.

17 A Okay. Closely associated with this
18 reasoning are the accounting principle that
19 revenues be matched with cost and the regulatory
20 principle that utility customers who benefit from
21 the consumption of plant pay for the costs of that
22 plant, no more, no less. The application of the
23 latter principles also requires that the estimated
24 cost of removal of plant be recovered over its
25 life.

1 Q Okay. Thank you. You have adopted
2 Mr. Adam's testimony in this case; is that
3 correct?

4 A Yes.

5 Q And Mr. Adam testified that his
6 problem with the standard method was that the net
7 salvage costs that it produced were greater than
8 actual net salvage, leading to what he referred to
9 as an overaccrual.

10 A That's correct.

11 Q And do you agree today with this
12 testimony that you adopted on August 20th?

13 A With regard to that. Yes.

14 Q Okay. Do you understand that based
15 on system growth and inflation, accrual for future
16 net salvage of current plant would naturally
17 exceed recent net salvage costs on a smaller base
18 of past plant?

19 A Given there's more plant, there's
20 more to retire.

21 Q More plant and inflation.

22 A I think that's an assumption, yes.

23 Q Okay. And do you understand that
24 this is the result of an accrual treatment versus
25 a cash treatment? In other words, the standard

1 method, in a situation where there is system
2 growth and inflation, the standard method will
3 result in a larger net salvage estimate than
4 current costs simply by virtue of the fact that it
5 -- it's being looked at on an accrual basis rather
6 than a cash basis?

7 A Okay, I thought -- there was two
8 questions there, so I wasn't -- maybe you should
9 -- maybe you could ask them --

10 Q Would you like me to restate them
11 one at a time? I'll be glad to try again.

12 A If you don't mind.

13 Q Okay. We established that based on
14 a situation where there is system growth and
15 inflation, the standard method's accrual for
16 future net salvage of current plant would
17 naturally exceed the net salvage costs on a
18 smaller base of past plant. Correct?

19 A Even if there's not growth, it will.

20 Q Just by virtue of inflation?

21 A No, just by virtue of -- I don't
22 know how to describe that. Those -- as you --
23 maybe as the system's maturing, those things will
24 as well occur, and that will -- use of the
25 standard approach still continues to provide more.

1 Q Okay. And -- and you understand
2 that this is a result of the standard method
3 applying an accrual treatment versus a look at
4 recent net salvage costs on a cash basis?

5 A On the accrual aspect of it, and
6 maybe this should be for accrual -- accrual --
7 total accrual concepts, I will defer that to Mr.
8 Oligschlaeger.

9 Q Well, I guess I'm not talking about
10 cash flow issues at this point, or -- or credit
11 rating issues. I just want to establish that the
12 standard approach looks at the plant that's in
13 service now and makes an attempt to estimate what
14 the costs will be to retire that plant.

15 A Well, I agree, but so does Staff's.
16 Because we have a reserve, it's still accruing.
17 So in this case, the reserve is still an accrual
18 mechanism.

19 Q Well, Staff's looks at the recent
20 past, the net salvage costs in the recent past,
21 and assumes the usage of those actual amounts from
22 the recent past to be used in the future by the
23 company. Right? In other words, in effect, a
24 cash basis. You agreed, I think, to all this with
25 Mr. Lowery.

1 A I think Mr. Adam is in essence cash
2 -- I think that because we haven't reserved it,
3 it's still accruing, but it's -- it tends to take
4 on a hybrid kind of feeling. But I would defer
5 that -- he -- the exact accrual to Mr.
6 Oligschlaeger.

7 Q Well, I think we're taking a step
8 backward, because I think you agreed with Mr.
9 Lowery that effectively the Staff's method is a
10 cash treatment of net salvage. Would you -- do
11 you agree with that?

12 MR. SCHWARZ: I'm going to object
13 because it, according to Mr. Zucker, it's been
14 asked and answered.

15 JUDGE DIPPELL: As long as she'll
16 answer --

17 MR. ZUCKER: It's now been answered
18 twice, two different ways, so I'd like to go for
19 two out of three.

20 JUDGE DIPPELL: Again, I'm not sure
21 she did answer it the second time, Mr. Zucker, but
22 I think you're safe just going with Mr. Lowery's
23 answer. The question has been asked and answered.

24 MR. ZUCKER: Okay. Very good.

25 Q (BY MR. ZUCKER) Given that the

1 difference in the amounts that come from the
2 standard method versus the amount that comes from
3 Staff method is caused by a difference between an
4 accrual treatment under the standard method and
5 the cash treatment under the Staff's method, isn't
6 your real issue the use of the -- that you would
7 rather use the cash treatment for net salvage
8 rather than the accrual treatment?

9 A No, I thought what -- the
10 substantiveness of the two are -- are close in the
11 dollars that it creates of what Mr. Adam did in
12 accruing for it, or putting it on an expense
13 basis. If that didn't answer the question, you
14 can ask me again. I apologize.

15 Q Mr. Adam was unclear whether the
16 difference between the standard method and the
17 recent net salvage levels was caused by net
18 salvage differences or differences in service
19 lives. Do you agree with me that that's what his
20 testimony said?

21 A Yes.

22 Q And Mr. Adam had no issue with any
23 particular estimate produced by the standard
24 method. Do you agree with that?

25 A I thought that he did.

1 Q Can you point to me where in his
2 testimony that he --

3 A Okay, so I'm clear as to what you're
4 -- can you repeat the question again?

5 Q Mr. Adam was, in his testimony, he
6 was disturbed with the standard method because it
7 came up with figures that were higher than recent
8 levels of net salvage. He was unclear whether
9 this difference was caused by differences in net
10 salvage or differences in service lives.

11 A I thought it was the overaccrual, he
12 was not able to identify, because there's such --
13 and it's a problem in our state. We need to get
14 it to where these are not commingled, and that
15 will help satisfy, I believe, what his confusion
16 was as to what amount was for the average service
17 life and which amount was for the net salvage
18 percentage.

19 Q But he didn't have any issue with
20 any particular estimate? He didn't identify
21 anything, he just said, I'm not sure what's
22 causing the difference between the standard method
23 and recent net salvage levels?

24 A Allow me -- I'll look at his
25 testimony. In talking with him, his concern -- I

1 mean, I know in talking with him, it wasn't
2 predictive, but whether that's laid out in the
3 testimony, I'll take time to look and see if --

4 Q All I want to know is what's in the
5 testimony. I'm not interested in the out of court
6 statements he may have made to you. May or may
7 not have made to you. Let me refer you to page 8
8 of his direct. Do you have it there?

9 A Yes.

10 Q Does he say in -- at line 13, it
11 appears to me that the net salvage part of the
12 depreciation rate formula has not been -- has not
13 historically been adjusted to charge the customer
14 the current net salvage cost. Since most accounts
15 have a negative net salvage, this condition has
16 led to an annual over recovery which has been
17 building in the accrual balance.

18 A Okay.

19 Q Another -- he goes on on line 18,
20 another conclusion could be that the computed
21 average service life is wrong.

22 MS. O'NEILL: Excuse me, could we
23 wait and let the witness answer the first
24 question?

25 MR. ZUCKER: I didn't ask a

1 question.

2 MS. O'NEILL: It appeared she was
3 trying to make a response, and I didn't get a
4 chance to hear that. Otherwise, I'm going to
5 object to compound question.

6 THE WITNESS: I think I got the
7 first --

8 MR. ZUCKER: I wasn't asking
9 questions yet, I was still reading the sentence
10 for her.

11 JUDGE DIPPELL: I think that perhaps
12 Ms. O'Neill is referring to the question that had
13 been asked before that the witness had not yet
14 answered.

15 MS. O'NEILL: Mm-hmm.

16 MR. ZUCKER: Okay.

17 JUDGE DIPPELL: That's fine if
18 you're starting -- starting fresh to direct her to
19 a point, I understand that. So go ahead.

20 MR. ZUCKER: That's what I'm doing.
21 Thank you, Your Honor.

22 JUDGE DIPPELL: Let him ask the
23 question again, starting with that.

24 Q (BY MR. ZUCKER) Okay. I'll finish
25 -- conclude my reading there at line 18, and then

1 I'll ask you the question again.

2 Another conclusion could be that the
3 computed average service life is wrong in those
4 cases where the retirement rate and the net
5 salvage data is much lower than the average
6 service life implies. It is possible that the
7 survivor curve has been misanalyzed and the
8 average service life understated.

9 A Okay.

10 Q So is what he's saying there that
11 he's not sure what the problem is, it could be net
12 salvage or it could be average service lives?

13 A He's saying that those are the
14 contributing factors to changes. Yes.

15 Q But he doesn't specifically identify
16 any particular estimate that's incorrect?

17 A Not in the text of his testimony.

18 Q And you haven't presented anything
19 in your testimony disputing any of Laclede Gas'
20 net salvage estimates. Is that correct?

21 A Well, um, I believe his work papers
22 is the demonstrative aspect of that.

23 Q And those are attached to his
24 testimony. Right?

25 A No, no, they're not.

1 Q Mr. Adam did not have an issue with
2 the known and measurable point that you've made
3 here in 1999; is that correct?

4 A It was my understanding that's the
5 pretext under what he was working. He was --

6 Q But his problem was that the
7 standard method produced a net salvage accrual
8 that's larger than the expense -- the expense
9 method. That was his real problem.

10 A Well, that is correct. I mean, in
11 lines 9 -- he -- he says the customer should be
12 paying only the current negative net salvage of
13 interim retirements. That in and of itself is the
14 concept of being able to measure, and with
15 reasonable precision, that is that concept.

16 Q You're aware that Laclede spends
17 approximately \$50 million a year on capital
18 assets?

19 A That's not something that comes into
20 my study, no. But it's been in testimony.

21 Q Okay. Do you have any reason to
22 doubt that testimony?

23 A No, I do not.

24 Q Is that amount known and measurable?

25 A Yes, it is.

1 Q And Laclede recovers that by
2 spreading that amount over the lives of those
3 assets?

4 A Yes, it does.

5 Q And that's based on average service
6 lives?

7 A Yes.

8 Q And isn't average service life an
9 estimate?

10 A It is with the caveat that it's an
11 estimate resulting from work that's empirical
12 studies in that area.

13 Q But the average service life is not
14 known and measurable?

15 A A life, no.

16 Q So, then, under your known and
17 measurable standard, why wouldn't Laclede collect
18 its entire \$50 million in the year it spends it?
19 In other words, the 50 million is known and
20 measurable, the lives aren't. You said we can't
21 work on estimates, we can't do -- we can't collect
22 things that aren't known and measurable.

23 So why don't we collect the 50
24 million that we spend every year in the -- in the
25 -- why don't we expense it?