Exhibit No.:
Issues: *Depreciation, Cost of Removal and Net Salvage*
Witness: *Rosella L. Schad, PE*
Sponsoring Party: *MoPSC Staff*
Type of Exhibit: *Supplemental Rebuttal Testimony*
Case No.: *GR-99-315*
Date Testimony Prepared: *September 10, 2004*

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

SUPPLEMENTAL REBUTTAL TESTIMONY

OF

ROSELLA L. SCHAD, PE

LACLEDE GAS COMPANY

CASE NO. GR-99-315

Jefferson City, Missouri
September 2004

****Denotes Highly Confidential Information****

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BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Laclede Gas Company's Tariffs to Revise Natural Gas Rate Schedules.	)))	Case No. GR-99-315

AFFIDAVIT OF ROSELLA L. SCHAD, PE

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Rosella L. Schad, PE, being of lawful age, on her oath states: that she has participated in the preparation of the following supplemental rebuttal testimony in question and answer form, consisting of 18 pages to be presented in the above case; that the answers in the following supplemental rebuttal testimony were given by her; that she has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of her knowledge and belief.

Rosella L. Schad, PE
Rosella L. Schad, PE

Subscribed and sworn to before me this 10th day of September 2004.

Toni M. Charlton
Notary

TONI M. CHARLTON
NOTARY SEAL
NOTARY PUBLIC
STATE OF MISSOURI

TONI M. CHARLTON
NOTARY PUBLIC STATE OF MISSOURI
COUNTY OF COLE
My Commission Expires December 28, 2004

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SUPPLEMENTAL REBUTTAL TESTIMONY

OF

ROSELLA L. SCHAD, PE

LACLEDE GAS COMPANY

CASE NO. GR-99-315

Q. Please state your name and business address.

A. My name is Rosella L. Schad, P.O. Box 360, Jefferson City, MO 65102.

Q. By whom are you employed and in what capacity?

A. I am employed by the Missouri Public Service Commission (PSC or Commission) as an Engineer in the Engineering and Management Services Department.

Q. Are you the same Rosella L. Schad who has previously filed supplemental direct testimony on behalf of the Missouri Public Service Commission in this case?

A. Yes.

Q. What is the purpose of your supplemental rebuttal testimony?

A. I will respond to the arguments made by Laclede Gas Company (Laclede) and Union Electric Company d/b/a AmerenUE (AmerenUE) witnesses regarding the ratemaking treatment for net salvage costs. These witnesses are: Warner L. Baxter, Martin J. Lyons, Jr., and Steven M. Fetter, AmerenUE; William M. Stout, AmerenUE and Laclede; and witnesses R. Lawrence Sherwin and Barry C. Cooper, Laclede. (Collectively, I will refer to Laclede and AmerenUE as the "Companies.")

Q. What is at issue in this case?

A. As I stated on page 2 of my supplemental direct testimony, the issue that remains in this case is the appropriate cost to remove retired property, one that is known and

measurable to a sufficient degree to be included in the rates charged to Laclede's customers. Staff's position is that collection of cost of removal dollars in rates should only be allowed when it is reasonably certain the amounts will be expended in the future to remove retired plant.

Q. What are the key arguments raised by the Companies in objection to Staff's position?

A. The significant areas of contradiction are:

1. Identification of a "Standard Approach" to treatment of net salvage that the Commission has used for decades.

2. Identification of intergenerational inequity imputed on future customers as a result of the use of Staff's approach to removal costs for mass property assets.

3. Identification of customer safeguards embedded in the "Standard Approach" to treatment of net salvage.

4. Identification of public policy implications resulting from using Staff's approach in developing cost of service revenue requirement.

5. Identification of financial and cash flow impacts on Missouri utilities.

Q. Will you address all of these concerns?

A. I will address items 1-4. Staff witness, Mark L. Oligschlaeger, will address item 5.

IDENTIFICATION OF A "STANDARD APPROACH" TO TREATMENT OF NET SALVAGE THAT THE COMMISSION HAS USED FOR DECADES.

Q. Can you give an explanation of the "Standard Approach" treatment of net salvage that the Commission is alleged to have "used for decades" as stated on page 12 of the supplemental direct testimony of AmerenUE witness Baxter?

A. Yes. On page 6 of his supplemental direct testimony, Mr. Lyons, states, "Net salvage is expressed as a percentage of plant retired by dividing the dollars of net salvage by the dollars of original cost of plant retired."

Dividing the net salvage percentage, as defined in Mr. Lyons' testimony, by the average service life of the plant asset account determines the depreciation rate for net cost of removal. Calculating the depreciation rate for cost of removal using the definition Mr. Lyons used for net salvage, is the concept the witnesses are referring to as the "Standard Approach." The "Standard Approach" results in the determination of an estimated value for future net cost of removal, which is then ratably recovered over the estimated service life of the plant asset account.

Applying the depreciation rate for net cost of removal times the plant asset account balance determines the annual depreciation expense for cost of removal. The depreciation rate for recovery of original cost is 100% divided by the average service life of the plant asset account. Applying the depreciation rate for recovery of original cost times the plant asset account balance determines the annual depreciation expense for recovery of original cost. The total depreciation rate is the summation of two rates: the depreciation rate for recovery of original cost plus the depreciation rate for cost of removal. Applying the total depreciation rate times the plant asset account balance determines the annual depreciation expense for a

plant asset account. Traditionally, the Commission's orders address only the total depreciation rate given as a percentage.

Staff calculates the net salvage percentage in a different manner from the "Standard Approach." Staff's method is to determine the proper net salvage percentage for an account that will generate an annual depreciation expense for cost of removal that equals the Company's ongoing level of cost of removal, using the Company's most recent history for cost of removal for the account being studied.

Q. Have utilities been ordered for decades to use the "Standard Approach" calculation to depreciate their plant assets, as stated by Mr. Baxter?

A. No.

Q. Will you provide historical information describing the depreciation rates Laclede has been ordered to use?

A. In Laclede Gas Light Company Case No. 5217, decided November 30, 1929, Laclede was ordered to set aside each year an amount equal to one and one-half percent of the investment cost of its depreciable property as a depreciation reserve fund. In Laclede Gas Light Company Case No. 11,618, decided September 18, 1953, Laclede was ordered a depreciation rate for each account. This was the first modification from the one and one-half percent of the investment cost of its depreciable property as a depreciation fund. Laclede was not ordered to use a "Standard Approach" to calculate its depreciation rates or more specifically, the component for net salvage.

In a subsequent case, Case No. 14,273, decided March 22, 1960, Laclede was ordered a depreciation rate for each account. Again, Laclede was not ordered to use a "Standard Approach" to calculate its depreciation rates. Schedules 1 through 6 to my testimony are

materials referencing depreciate rates for both Laclede and AmerenUE from 1965 thru 1987. These schedules indicate that neither Laclede Gas Company nor AmerenUE were ever required to develop or use depreciation rates based on a "Standard Approach." In Laclede Gas Company Case No. GR-78-148, Laclede was again ordered a depreciation rate for each account. As in previous cases, Laclede was not ordered to use a "Standard Approach" to calculate the net salvage component of its depreciation rates. Subsequent to 1978 and up to and including Laclede Case No. GR-98-374, Laclede was ordered depreciation rates based on Stipulations And Agreements. None of the Commission orders in these Stipulations specified how the net salvage component in the depreciation rate was to be determined.

Q. Has Mr. Baxter identified and been able to support a "Standard Approach" treatment of net salvage that the Commission has used for decades?

A. No. On page 12 of his supplemental direct testimony, he states:

> The problem is that past depreciation rates, which were approved by this Commission and used by Missouri utilities to accumulate the depreciation reserve, were based on the standard treatment of net salvage that the Commission has used for decades.

In fact he has not provided any reference to even one Laclede or AmerenUE order requiring it to accumulate the depreciation reserve based on the "Standard Approach" of net salvage, and has also failed to demonstrate that the Commission has used a "Standard Approach" for decades. As I have shown, depreciation rates were a flat percent of plant investment until the 1950's.

Q. On page 3 of his supplemental direct testimony, Mr. Lyons states:

> In stark contrast with the standard approach, Staff's approach to net salvage is inconsistent with USOA requirements, is inconsistent with the standard regulatory practice recommended by the National Association of Regulatory Utility Commissioners ("NARUC"), and is not supported by recognized authorities in the field.

Please address each of these assertions.

A. The 1992 FERC Uniform System of Accounts (USOA) prescribed for Natural Gas Companies does not require the net salvage component of the depreciation rate calculation to be derived according to a "Standard Approach." Depreciation, service value, and net salvage are all described, but no authorized formula for the net salvage component (net salvage percentage) of the depreciation rate calculation is included.

According to the 1996 National Association of Regulatory Utility Commissioners' Public Utility Depreciation Practices, p. 157:

> Some commissions have abandoned the above procedure and moved to current-period accounting for gross salvage and/or cost of removal. In some jurisdictions gross salvage and cost of removal are accounted for as income and expense, respectively, when they are realized. Other jurisdictions consider only gross salvage in depreciation rates, with the cost of removal being expensed in the year incurred.

Depreciation consultants are not registered by an authoritative board, which governs the practice and specifies generally accepted depreciation principles. In fact, depreciation consultants have developed the net salvage component in the depreciation rate calculation in various manners. Development of recommended net salvage ratios by depreciation consultant L. W. Loos in Empire District Electric Case No. ER-2001-299 included the effect of: average experienced net salvage ratios over past periods, interim retirements associated with interim (additions) that are expected to occur in order for the plant to realize expected service life, industry averages, estimated final retirement cost of removal of life span plant, and engineering judgment. In addition to the average service life component and the net salvage component, another component for depreciation reserve variance has been entered into the depreciation rate calculation.

Depreciation consultant T. J. Sullivan noted on page 2 of his "Report on Depreciation Accrual Rates" for Missouri Gas Energy, Case No. GR-2004-0209:

> The annual depreciation expense represents the annual charge against income associated with the loss of service value of utility equipment. Historically, a number of different methods have been used by gas utilities to determine the level of depreciation expense to be charged against current income. Among the more common are:
>
> 1. A percentage of the investment in depreciable property.
>
> 2. A direct appropriation by management.
>
> 3. An amount equal to the original cost investment retired during the year.
>
> 4. A percentage of revenues.

Further, on page 12, Mr. Stout states:

> … Rather than developing a net salvage allowance based on the ratio of net salvage to the original cost of the plant retired, the ratio is based on the ratio of an annual allowance to total plant in service.

The evidence shown here is that depreciation consultants are not consistent with how the net salvage percentage should be calculated.

Another depreciation consultant in past Missouri rate cases has addressed a letter to the membership of The Society of Depreciation Professionals that summarizes arguments for and against proposals to require cash or other deferral mechanisms for salvage and/or cost or removal, and various state regulators' responses to such arguments (attached as Schedule 8 to this testimony). As he noted, "For the most part, the parties in the proceedings were represented by consultants."

Q. On page 19 of his supplemental direct testimony, Mr. Baxter states, "As Mr. Lyons explains in his testimony, time-tested analytic approaches have been employed to ensure reasonable accuracy of the estimated service lives and net salvage values used in the

depreciation accounting and ratemaking processes." Did either Mr. Baxter or Mr. Lyons provide the historical data and associated analyses supporting these time-tested analytic approaches for net salvage values?

A. No. As illustrated in the Report and Order of The Empire District Electric Company Case No. 12,471, decided December 24, 1952, the depreciation reserves for electric and water assets were to be allocated to the respective plant accounts for electric and water properties. It wasn't until the 1950's in Missouri that for all utilities (electric, steam, gas and water) depreciation was even allocated by plant account, rather than by a flat composite rate. This indicates that not even 50 years have passed since depreciation was first calculated for individual plant accounts and provided for an adjustment for net salvage. In fact this adjustment for net salvage has never been recorded by utilities for amounts collected or segregated from other funds to track the level of collections to dollars actually spent.

Without adequate record keeping or segregation of net cost of removal dollars collected, there can be no way to ensure intergenerational equity or safeguards for the customers, issues I will address in more detail later. To suggest that the "Standard Approach" has been utilized for decades in this state, as Mr. Baxter has indicated, and that the "Standard Approach" employs reasonable accuracy in estimating net salvage values is unsupported by the record in this case or by this Commission's Reports and Orders.

Q. Relying on a definition of net salvage provided on page 6 of his testimony, Mr. Lyons continues on page 8:

> Under the standard regulatory approach the proper annual accrual for net salvage in depreciation rates is determined by estimating the net salvage values of assets currently used to serve customers and allocating those net salvage values over the estimated life of the assets.

What benefit do the utilities get by calculating the accrual for net salvage by dividing the dollars of net salvage by the dollars of original cost of plant retired?

A. The benefit to the utilities for the "proper" definition of net salvage percentage to be so defined is that it generates very large annual depreciation accruals. Because depreciation accruals are expenses, that do not require an outlay of cash, the utilities receive large amounts of cash in excess of what they actually spend. Generating large amounts of cash in this manner is the benefit that the utilities seek. Staff witness Mark Oligschlaeger will discuss this issue in his supplemental rebuttal testimony.

Q Will you illustrate how the "proper" definition of net salvage percentage generates very large annual depreciation accruals?

A. Yes. Assume that a company spends $100,000 to remove a 20-foot section of main that originally cost $50,000, there is no salvage, and the utility inventory is first in-first out (FIFO), meaning the oldest plant inventory is retired from the books. Even if the 20-foot section is only 10 years old, the original cost retired from the books (perhaps pipe from the 1920's) is used in the ratio. Original cost from the 1920's is substantially less than recent history. This is one factor (FIFO compounded with inflation) that creates a reduced denominator in the ratio, resulting in a much higher ratio. Thus, the "proper" ratio is now $100,000 divided by $50,000, equaling 200%. If the plant account balance is $300,000,000 and the average service life of the main account is 75 years, the annual depreciation accrual for cost of removal generated by the "proper" ratio is $8,000,000. The "Standard Approach" would generate $8,000,0000 annually as shown below:

$$\$8,000,000 = (200\% / 75) * \$300,000,000$$

It may not be reasonable to assume that the net salvage experience for a small span of time applies to all plant in the future. More specifically, there have been no empirical studies that develop any relationship or correlation between the "proper" ratio that Laclede and AmerenUE wants and future costs of removal that will actually be spent. The "Standard Approach" supported by both Laclede and AmerenUE creates intergenerational inequity.

In contrast, if the company spent $100,000 to remove a 15-foot section of main, which, in this example, does not constitute a retirement unit, the $100,000 would be captured in full as a maintenance expense for the year. The future customer receives all the benefit of this expenditure yet pays nothing. This is not consistent with intergenerational equity.

The company receives the windfall of $7,900,000 by using the "Standard Approach" for determining the net salvage percentage in the depreciation rate. When a utility attempts to reduce the average service life of an account, the use of the "Standard Approach" magnifies the over-accrual dilemma.

Q. What is the effect of using the "proper" annual accrual that Mr. Lyons suggests?

A. An excessive annual over-accrual booked over several years results in large amounts of cash for the company.

Q. Isn't Staff concerned about this overcharging of customers?

A. Certainly. This concern caused Staff witnesses to address the issue in 1990 and continue to do so today. As the Commission's Report and Order noted in Missouri Public Service Company Case No. ER-90-101, the method employed by Staff/Public Counsel is reasonable and consistent with methods utilized in previous cases.

IDENTIFICATION OF INTERGENERATIONAL INEQUITY IMPUTED ON FUTURE CUSTOMERS AS A RESULT OF USE OF STAFF'S APPROACH TO REMOVAL COSTS FOR MASS PROPERTY ASSETS.

Q. On page 3 of his supplemental direct testimony, witness R. Lawrence Sherwin states:

> In contrast, the Staff's method expenses the net salvage costs that have been incurred in the past in connection with those utility facilities that have already been retired and therefore no longer serving customers. As a result, the Staff's method makes no effort to estimate or reflect in rates the net salvage costs that decades worth of data indicate will be experienced in connection with the retirement of existing facilities.

Are you aware of a collection of "decades" worth of data identifying the future cost of retiring existing facilities?

A. No. In fact such data would be required to support Mr. Baxter's assertion on page 7 of his testimony that says: "Staff's proposal creates inter-generational equity problems." Intergenerational equity is achieved by associating costs of service with the customers who use the service. In order to attain intergenerational equity, the costs must be known amounts, not subject to change, and identifiable as when they will or have been incurred. In addition, it is necessary to keep a record system or segregation of funds to support the amounts and timing of collections of funds and the amounts and timing of costs incurred. Accounting conventions such as FIFO misstates the amounts and timing of costs incurred.

Q. Can you give an example of how the Staff's approach is better to achieve intergenerational equity?

A. Yes. In instances where plant is abandoned or sold in the future, Staff's method ensures that current customers do not pay excessive amounts for future costs of removal through the depreciation rates that are never incurred. ** _____

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Q. Are there other ways intergenerational inequity can occur?

A. Yes. Utilities code retirement of plant according to units of property defined in the company's property unit catalog as required by MoPSC Rule 4 CSR 240-40.040(2)(B). For example, if 20 feet of main is one unit, the retirement and replacement of a length of pipe less than 20 feet is charged to maintenance expense for the year. If in a given year the utility retires and replaces 15 feet of main in order to keep the system functional, a customer will pay the entire cost in maintenance expense for the year, even though the main will continue to provide service for not only this customer but future customers. If in the same system, 20 feet is retired, removed, and replaced with a new 20-foot section, the main will continue to provide service. Current customers are realizing continued service due to retiring and removing plant for which there was a cost of removal expense. By using Staff's approach for cost of removal expense, current customers are paying those removal costs that are integral to continued service even though plant has retired. As an on-going level of cost of removal, the amount reflected by Staff in customer rates should reflect the known and measurable

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amounts currently incurred by the utility as noted by Staff witness, Melvin T. Love, in Missouri Public Service Company Case No. ER-90-101 and by Staff witness, Paul W. Adam in this case.

Q Have you reviewed Mr. Stout's comparison, on page 18 and Schedule WMS-2 of his supplemental direct testimony, of the revenue requirement for the two approaches?

A Yes. Mr. Stout's approach uses assumptions that estimated future costs of removal will actually be incurred at precisely the levels indicated. These assumptions have not proved to be true for any utility operating in the state of Missouri. Staff's approach recognizes to the extent that estimated future costs, including final retirements of mass asset property and final retirements of life span property, are speculative and not known and measurable they should not be included in the depreciation rate. Speculative costs have been addressed in Missouri Public Service Case No. ER-97-394 Report and Order, "The Commission finds that terminal net salvage costs are speculative and not known and measurable and therefore may not be included in current rates." Mr. Stout's assumptions for estimated future costs of removal for mass asset property are as speculative as those identified by the Commission in Case No. ER-97-394.

It is important to recognize that even Laclede has found estimated future cost of removal for mass property accounts to be speculative as they have shown on pages 39-40 of Laclede Gas Company's Securities and Exchange Commission, Form 10-K for the Fiscal Year Ended September 30, 2003. It states:

> The FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations," … There are legal obligations related to final abandonment of the Utility's gas distribution system. However, these obligations related to mass property and other distribution system assets generally continue in perpetuity and can not be measured under

> SFAS No. 143 because of indeterminate settlement dates and cash flow estimates.

Q. Does witness Steven M. Fetter, on page 8 of his supplemental direct testimony, assert that another jurisdiction's views about dismantlement costs of generating stations are policies that provide guidance for the appropriate depreciation treatment of mass property accounts at issue in this proceeding?

A. Yes. He also notes on page 7 that the definitions within the gas portion of the USOA are similar in language and intent as these electric provisions. However, the Commission addressed dismantlement costs of generating facilities in Case No. ER-97-394. Except for nuclear decommissioning costs, which are deposited in a sinking fund, the Missouri Commission has not authorized utilities in Missouri to collect final retirement costs of life span plant. Therefore, Mr. Fetter's attempts to suggest guidance for cost of removal on mass property accounts from experiences in life span property cannot be utilized as the Commission has previously ruled that no final removal costs are to be included in the depreciation rate for life span property. Mr. Fetter's attempts are unwarranted.

Q. On page 4 of witness Barry Cooper's supplemental direct testimony, he states:

> Indeed, the fact that the Commission has not yet been able to provide an adequate explanation of why Staff's method is appropriate – despite repeated efforts to do so in the five plus years since this issue was first addressed by the Commission – only reinforces the view that Staff's method is fundamentally flawed.

How long, to your knowledge, has Staff identified the need to propose collections for cost of removal through depreciation expense reflecting current expenditures?

A In Missouri Public Service Case No. ER-90-101 Staff witness Melvin T. Love filed testimony that recommended current levels of cost of removal rather than a net salvage amount based upon future estimates. In the Commission's Report and Order, the

Commission found, "The method employed by Staff/Counsel is reasonable and consistent with methods utilized in previous rate cases. Company has failed to show that there is a reason to modify this approach." In stark contrast to the testimonies filed by the witnesses in this case, the Report and Order in Case No. ER-90-101 contradicts their assertion that Staff has set about proposing a new approach. Furthermore, this Report and Order reflects the collective judgment and long experience of this Commission regarding how net salvage costs should be handled for public utilities.

Q. After Case No. ER-90-101, did Staff continue to recommend that the magnitude of the accrual for cost of removal be reduced to match the experience of the past?

A. Yes. In Missouri Public Service Case No. ER-93-37 Staff witness Melvin T. Love maintained the same position.

IDENTIFICATION OF CUSTOMER SAFEGUARDS EMBEDDED IN THE "STANDARD APPROACH" TO TREATMENT OF NET SALVAGE

Q. How would you address Mr. Baxter's concern with Staff amortizing over–accruals in current rates?

A. When Staff recognizes that current customers have been overcharged for removal costs, i.e. the annual depreciation accrual is collecting excessive amounts over and above the known and measurable cost of removal, Staff recommends implementing a negative amortization. This recommendation has only occurred after careful consideration of the magnitude and duration of over-accrual.

Q. On page 10 of his testimony, Mr. Lyons provides his view of safeguards of the "Standard Approach." He states "The standard approach incorporates safeguards that fully and effectively protect both customers and utilities from potentially adverse effects

associated with estimating depreciation lives and net salvage." Can you illustrate how Staff's approach provides the better safeguards?

A. Yes. The "Standard Approach" supported by both AmerenUE and Laclede fails to provide mechanisms that ensure dollars collected are available in the event future expenditures for cost of removal occur. Staff's approach fully and effectively safeguards current customers from being overcharged for cost of removal, and ensures that the utility receives dollars from its customers to cover its on-going expenditures.

Q. Mr. Stout indicates on page 29 of his testimony that he compared the composite depreciation rates for Laclede's total gas plant to the corresponding composite depreciation rates for the other investor-owned gas utilities in the United States. Do you have any concerns with generalized comparisons?

A. Yes. Comparisons of one utility's depreciation rates with those effective at other utilities in the same industry are not persuasive as to the reasonableness or unreasonableness of the rates under observation. Before a conclusion can be reached from such a comparison, you must know and understand all factors affecting plant additions and retirements. This requires inquiry into the methods of operations in the various utilities; the various types of property used in the construction of a system; the conditions under which assets are being retired from service; the accounting conventions utilized to associate removal costs with retired plant or capitalized with new construction costs; threshold levels for capitalization; the use of FIFO, LIFO (Last In, First Out), or some other inventory system, classification of retirement units in the Continuing Plant Inventory Record; and the quality of data maintained for depreciation analysis.

Q. Can you provide an example where a Missouri-regulated provider of natural gas services books its cost of removal in such a manner that a comparison of it to other utilities may not provide conclusion as to the reasonableness of its depreciation rate for cost of removal?

A. Yes. Highly Confidential Schedule 7 is AmerenUE's responses to Staff Data Requests 4601, 4602, 4603, and 4604 in Case No. GR-2000-512. ** _____

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IDENTIFICATION OF PUBLIC POLICY IMPLICATIONS RESULTING FROM USING STAFF'S APPROACH IN DEVELOPING COST OF SERVICE REVENUE REQUIREMENT

Q. On page 23 of his testimony, Mr. Baxter draws conclusions relating to public policy. Can you explain the purpose of regulatory depreciation?

A. Yes. The purpose of regulatory depreciation in developing the cost of service revenue requirement is the recovery of original cost of plant assets ratably over the life of the assets. In an economic era when positive salvage prevailed, the original cost was reduced by any net salvage that could be received at the end of its useful life. It was noted in St. Louis County Gas Company Case No. 9632, decided June 1, 1943 that removal costs were charged to maintenance expense prior to January 1, 1932, the effective date of revised Uniform System of Accounts. Following January 1, 1932 the charges for property retirements were adjusted to include removal costs. It appears that it was not until the 1960s that the cost to remove plant exceeded salvage and was addressed because of the impact on annual depreciation accrual. It was noted in Laclede Gas Co. Case No. 14,273, decided March 22,

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1960, that increases in depreciation accrual were resulting from an increase in the cost of removal and the consequent decrease in net salvage. Regulatory depreciation analysis does not include cash flow or financial factors. Staff witness Oligschlaeger addresses cash flow and financial considerations associated with this issue in his supplemental rebuttal testimony. Only to the extent that the Commission makes these cash flow and financial considerations, as was done in St. Louis County Water Company Case No. WR-2000-844, is regulatory depreciation integrated with public policy matters.

Q. Does this conclude your supplemental rebuttal testimony?

A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

DEPRECIATION AUTHORITY ORDER NO. 41

In the matter of prescribing depreciation)
accrual rates for the Laclede Gas Company)
of St. Louis, Missouri.)

As provided for in Section 393.240 of the Missouri Revised Statutes, 1959, the Commission's Engineering Staff has made its study and investigation of the several classes of property of the Laclede Gas Company and has ascertained, determined, and fixed the recommended rates of depreciation of the several classes of property and has recommended that the Commission require that those rates be prescribed for accruing depreciation credits to the depreciation reserve until further order of the Commission.

The Commission, having considered the recommended rates, finds that such rates are proper and adequate.

It is, therefore,

ORDERED: 1. That the Laclede Gas Company be and it is hereby ordered to adopt the following depreciation accrual rates:

Account Number	Description of Account	Accrual Rate %
MANUFACTURED GAS PRODUCTION PLANT		
305.00	Structures & Improvements	3.44
307.00	Other Power Equipment	3.04
311.00	Liquified Petroleum Gas Equipment	3.36
320.00	Other Equipment	2.47
UNDERGROUND STORAGE PLANT		
350.30	Storage Rights	3.55
350.40	Rights of Way	3.61*
351.20	Compressor Station Structures	2.72
351.40	Other Structures	3.81
352.00	Wells	4.08
353.00	Lines	4.10
354.00	Compressor Station Equipment	3.47
355.00	Measuring & Regulating Equipment	4.53
356.00	Purification Equipment	4.14
357.00	Other Equipment	3.88
	* After exclusion of oil rights being amortized.	
LOCAL STORAGE PLANT		
361.00	Structures & Improvements	2.93
362.00	Gas Holders	2.49
363.00	Other Equipment	4.65
DISTRIBUTION PLANT		
375.10	Structures & Improvements, Measuring & Regulating Stations	1.73
375.20	Structures & Improvements, Service Centers & Storerooms	1.83
375.30	Structures & Improvements, Garages	2.04
376.10	Mains, Steel	4.00
376.20	Mains, Cast Iron	1.26
378.00	Measuring & Regulating Station Equipment, General	3.07
379.00	Measuring & Regulating Station Equipment, City Gate	3.05
380.10	Services, Steel	4.56
380.20	Services, Copper	3.40
381.00	Meters	2.36

DISTRIBUTION PLANT (continued)

383.00	House Regulators	2.33
385.00	Commercial & Industrial Measuring & Regulating Equipment	2.64
386.10	Other Property on Customers' Premises, LPG Systems	15.27
387.00	Other Equipment (Street Lights)	3.89

GENERAL PLANT

390.00	Structures (Main Office Building)	1.79
391.00	Office Furniture & Equipment	4.40
392.10	Transportation Equipment, Autos	15.57
392.20	Transportation Equipment, Trucks	10.55
393.00	Stores Equipment	4.21
394.00	Tools, Shop and Garage Equipment	4.55
395.00	Laboratory Equipment	4.42
396.00	Power Operated Equipment	8.72
397.00	Communications Equipment	8.58
398.00	Miscellaneous Equipment	5.65

ORDERED: 2. That beginning January 1, 1965, the Laclede Gas Company be and it is hereby ordered to accrue depreciation expense at the component rates set out in "ORDERED: 1." above.

ORDERED: 3. That the Laclede Gas Company upon receipt of this Order, shall notify the Commission within ten (10) days after the effective date hereof whether or not the terms of this Order will be accepted and obeyed.

ORDERED: 4. That this Order shall take effect on April 9, 1965, and that the Secretary of the Commission shall serve a certified copy of same upon said utility.

APPROVED:

Commissioners

BY THE COMMISSION

Warren G. Taylor
Secretary

(S E A L)

Dated at Jefferson City, Missouri,
this 29th day of March , 1965.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

DEPRECIATION AUTHORITY ORDER NO. 41.01

In the matter of prescribing depreciation)
accrual rates for the Laclede Gas Company)
of St. Louis, Missouri.)

As provided for in Section 393.240 of the Missouri Revised Statutes, 1959, the Commission's Engineering Staff has made its study and investigation of the several classes of property of the Laclede Gas Company and has ascertained, determined, and fixed the recommended rates of depreciation of the several classes of property and has recommended that the Commission require that those rates be prescribed for accruing depreciation credits to the depreciation reserve until further order of the Commission.

The Commission, having considered the recommended rates, finds that such rates are proper and adequate.

It is, therefore,

ORDERED: 1. That the Laclede Gas Company be and it is hereby ordered to adopt the following depreciation accrual rates:

Account Number	Description of Account	Accrual Rate %
MANUFACTURED GAS PRODUCTION PLANT		
305.00	Structures & Improvements	3.44
307.00	Other Power Equipment	3.04
311.00	Liquified Petroleum Gas Equipment	3.36
320.00	Other Equipment	2.47
UNDERGROUND STORAGE PLANT		
350.30	Storage Rights	3.55
350.40	Rights of Way	3.61*
351.20	Compressor Station Structures	2.72
351.40	Other Structures	3.81
352.00	Wells	4.08
353.00	Lines	4.10
354.00	Compressor Station Equipment	3.47
355.00	Measuring & Regulating Equipment	4.53
356.00	Purification Equipment	4.14
357.00	Other Equipment	3.88
	* After exclusion of oil rights being amortized.	
LOCAL STORAGE PLANT		
361.00	Structures & Improvements	2.93
362.00	Gas Holders	2.49
363.00	Other Equipment	4.65
DISTRIBUTION PLANT		
375.10	Structures & Improvements, Measuring & Regulating Stations	1.73
375.20	Structures & Improvements, Service Centers & Storerooms	1.83
375.30	Structures & Improvements, Garages	2.04
376.10	Mains, Steel	4.00
376.20	Mains, Cast Iron	1.26
378.00	Measuring & Regulating Station Equipment, General	3.07
379.00	Measuring & Regulating Station Equipment, City Gate	3.05

DISTRIBUTION PLANT (continued)

380.10	Services, Steel	4.56
380.20	Services, Copper	3.40
381.00	Meters	2.36
383.00	House Regulators	2.33
385.00	Commercial & Industrial Measuring & Regulating Equipment	2.64
386.10	Other Property on Customer's Premises, LPG Systems	15.27
387.00	Other Equipment (Street Lights)	3.89

GENERAL PLANT

390.00	Structures (Main Office Building)	1.79
391.00	Office Furniture & Equipment	4.40
391.10	Data Processing Systems	14.00
392.10	Transportation Equipment, Autos	15.57
392.20	Transportation, Equipment, Trucks	10.55
393.00	Stores Equipment	4.21
394.00	Tools, Shop and Garage Equipment	4.55
395.00	Laboratory Equipment	4.42
396.00	Power Operated Equipment	8.72
397.00	Communications Equipment	8.58
398.00	Miscellaneous Equipment	5.65

ORDERED: 2. That beginning January 1, 1967, the Laclede Gas Company be and is hereby ordered to accrue depreciation expense at the component rates set out in "ORDERED: 1." above.

ORDERED: 3. That the Laclede Gas Company upon receipt of this Order, shall notify the Commission within ten (10) days after the effective date hereof whether or not the terms of this Order will be accepted and obeyed.

ORDERED: 4. That this Order shall take effect on August 15, 1967, and that the Secretary of the Commission shall serve a certified copy of same upon said utility.

APPROVED:

W. R. Clark

Charles J. Fain

Missouri J. Jones

Howard S. Elliott

Commissioners

BY THE COMMISSION

Sam L. Manley
Secretary

(S E A L)

Dated at Jefferson City, Missouri,
this 4th day of August, 1967.

DISTRIBUTION PLANT (Continued)

376.10	Mains, Steel	4.00
376.20	Mains, Cast Iron	1.26
378.00	Measuring & Regulating Station Equipment, General	3.07
379.00	Measuring & Regulating Station Equipment, City Gate	3.05
380.10	Services, Steel	4.56
380.20	Services, Copper	3.40
381.00	Meters	2.36
383.00	House Regulators	2.33
385.00	Commercial & Industrial Measuring & Regulating Equipment	2.64
386.10	Other Property on Customer's Premises, LPG Systems	15.27
387.00	Other Equipment (Street Lights)	3.89

GENERAL PLANT

390.00	Structures (Main Office Building)	1.79
391.00	Office Furniture & Equipment	4.40
391.10	Data Processing Systems	14.00
392.10	Transportation Equipment, Autos	15.57
392.20	Transportation, Equipment, Trucks	10.55
393.00	Stores Equipment	4.21
394.00	Tools, Shop and Garage Equipment	4.55
395.00	Laboratory Equipment	4.42
396.00	Power Operated Equipment	8.72
397.00	Communications Equipment	8.58
398.00	Miscellaneous Equipment	5.65

ORDERED: 2. That beginning October 1, 1970, the Laclede Gas Company be, and is, hereby ordered to accrue depreciation expense at the component rates set out in Ordered 1 above.

ORDERED: 3. That the Laclede Gas Company, upon receipt of this Order, shall notify the Commission within ten (10) days after the effective date hereof whether or not the terms of this Order will be accepted and obeyed.

ORDERED: 4. That this Order shall take effect on October 5, 1971 and that the Secretary of the Commission shall serve a certified copy of same upon said utility.

BY THE COMMISSION

Sam L. Manley

Sam L. Manley
Secretary

APPROVED:

Commissioners

(S E A L)

Dates at Jefferson City, Missouri,

this 24th day of September, 1971.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

DEPRECIATION AUTHORITY ORDER NO. 41.02

In the matter of prescribing depreciation)
accrual rates for the Laclede Gas Company)
of St. Louis, Missouri.)

As provided for in Section 393.240 of the Missouri Revised Statutes, 1969, the Commission's Engineering Staff has made its study and investigation of the several classes of property of the Laclede Gas Company and has ascertained, determined, and fixed the recommended rates of depreciation of the several classes of property and has recommended that the Commission require that those rates be prescribed for accruing depreciation credits to the depreciation reserve until further order of the Commission.

The Commission, having considered the recommended rates, finds that such rates are proper and adequate.

It is, therefore,

ORDERED: 1. That the Laclede Gas Company be, and it is, hereby ordered to adopt the following depreciation accrual rates:

Account Number	Description of Account	Accrual Rate %
MANUFACTURED GAS PRODUCTION PLANT		
305.00	Structures & Improvements	3.44
307.00	Other Power Equipment	3.04
311.00	Liquified Petroleum Gas Equipment	3.36
320.00	Other Equipment	2.47
UNDERGROUND NATURAL GAS STORAGE PLANT		
350.20	Rights of Way	3.61*
351.20	Compressor Station Structures	2.72
351.40	Other Structures	3.81
352.00	Wells	4.08
352.10	Storage Leaseholds and Rights	3.55
352.20	Reservoirs	4.08
352.30	Non-Recoverable Natural Gas	4.00
353.00	Lines	4.10
354.00	Compressor Station Equipment	3.47
355.00	Measuring & Regulating Equipment	4.53
356.00	Purification Equipment	4.14
357.00	Other Equipment	3.88
	*After exclusion of oil rights being amortized.	
OTHER NATURAL GAS STORAGE PLANT		
361.00	Structures & Improvements	2.93
362.00	Gas Holders	2.49
363.30	Compressor Equipment	4.65
DISTRIBUTION PLANT		
375.10	Structures & improvements, Measuring & Regulating Stations	1.73
375.20	Structures & Improvements, Service Centers & Storerooms	1.83
375.30	Structures & Improvements, Garages	2.04

SCHEDULE 4

HAS BEEN DEEMED

HIGHLY CONFIDENTIAL

IN IT'S ENTIRETY.

Missouri Public Service Commission

Area Code 314
751-3234

P.O. BOX 360
JEFFERSON CITY
MISSOURI 65102

October 14, 1987

Mr. M. A. Wyka, Manager
Property Accounting Department
Union Electric Company
P. O. Box 149
St. Louis, MO 63166

Dear Mr. Wyka:

Please find enclosed the worksheet entitled "UEGAS.WK1". This worksheet states the composite depreciation rates for the total of Union Electric's former gas subsidiaries, Missouri Power and Light, Missouri Edison, and Missouri Utilities. These composite rates were computed using Staff's witness Kelly J. Riley's Accounting Schedule 3 in Case No. GR-87-62 and the enclosed worksheet entitled "Annualized Depreciation Gas Plant in Service by Subsidiary Division".

The composite rates were computed on worksheet "UEGAS.WK1" using direct weighting. The formula is as follows:

$$\text{rate for account} = \frac{\sum (\text{plant \$} * \text{division depr. rate})}{\text{total plant investment}}$$

If you concur with these rates and the manner in which they were computed, please advise us in writing. Upon receipt of your concurrence, the Staff will recommend the Commission prescribe these composite rates by a Depreciation Authority Order.

Thank you.

Sincerely,

Steven R. Coon

Steven R. Coon
Depreciation Engineer

SRC:ljm

Enclosure

STATE OF MISSOURI
PUBLIC SERVICE COMMISSION
At a Session of the Public Service Commission held at its office in Jefferson City on the 24th day of November, 1987.

DEPRECIATION AUTHORITY ORDER NO. 164

In the matter of prescribing depreciation accrual rates for the Union Electric Company (Gas Operations).

DEPRECIATION AUTHORITY ORDER

As provided for in Section 393.240 of the Missouri Revised Statutes, 1986, the Commission's Engineering Staff has made its study and investigation of the several classes of property of said utility and has ascertained, determined, and fixed the recommended rates of depreciation of the several classes of property for accruing depreciation credits to the depreciation reserve until further order by the Commission.

It is, therfore,

ORDERED: 1. That the said utility be, and it is, hereby ordered to adopt the following depreciation accrual rates beginning January 1, 1988:

Acct. No.	Description of Account	Annual Rate Percent
	INTANGIBLE PLANT	
301	Organization	--
302	Franchises and Consents	--
	MANUFACTURED GAS PRODUCTION PLANT	
304	Land	--
305	Structures and Improvements	2.38
306	Boiler Plant Equipment	2.55
311	Liquified Petroleum Gas Equipment	2.79
	TRANSMISSION PLANT	
365	Land and Land Rights, Rights of Way	--
366	Structures and Improvements	2.86
367	Mains	2.11
369	Measuring and Regulating Station Equipment	2.65
	DISTRIBUTION PLANT	
374	Land and Land Rights	--
375	Structures and Improvements	2.04
376	Mains	1.62
378	Measuring & Regulating Station Equipment - General	2.61
379	Measuring & Regulating Station Equipment - City Gate Check Station	2.61
380	Services	4.61
381	Meters	2.25
382	Meter Installations	3.17

383	House Regulators	2.66
384	House Regulator Installations	2.93
385	Industrial Measuring & Regulating Station Equipment	3.05
386	Other Property on Customers' Premises	3.30
387	Other Equipment	3.36
	GENERAL PLANT	
390	Structures and Improvements - Miscellaneous	2.13
391	Office Furniture and Equipment	4.48
392	Transportation Equipment	7.02
393	Stores Equipment	5.20
394	Tools, Shop and Garage Equipment	4.67
395	Laboratory Equipment	4.60
396	Power Operated Equipment	5.86
397	Communication Equipment	8.39
398	Miscellaneous Equipment	7.69

ORDERED: 2. That the said utility be, and it is, hereby ordered to accrue depreciation expenses at the component rates set in "ORDERED: 1." above.

ORDERED: 3. That this Order shall be effective ten (10) days after the date of this Order, and that the Secretary of the Commission shall serve a certified true copy of same upon said utility.

By The Commission

Harvey G. Hubbs
Secretary

(S E A L)
Steinmeier, Chm., Musgrave,
Mueller, Hendren, and Fischer,
CC., Concur.

SCHEDULE 7

HAS BEEN DEEMED

HIGHLY CONFIDENTIAL

IN IT'S ENTIRETY.

June 10, 2004

TO: Membership of the Society of Depreciation Professionals

FROM: John Ferguson, Chairman, SDP Current Issues Committee

This is another in the series of periodic letters to the membership in which issues that may be of interest are presented and/or discussed. Several Society members have agreed to assist me to identify such issues, but there is no intent to limit member input to these members. Therefore, ideas and materials from other members would be welcome. Distribution of these periodic letters is by email from Rod Daniel, and each is posted on the SDP web site (www.depr.org).

Please recognize that the thoughts expressed here are mine, not the Current Issues Committee members. I encourage anyone with additional or different thoughts to submit them to me at johnferg@swbell.net for consideration for a future letter on issues that may be of interest to SDP members.

Prior Committee letters have addressed the near-term and long-term impacts of the decrease in depreciation rates that would result from shifting from an accrual basis to a cash basis for salvage and/or cost of removal, pointing out that the initial revenue requirement impact reverses in the long-term. The most recent such discussion was in the March 31, 2004 Committee letter.

The remainder of this Committee letter addresses arguments for and against proposals to require cash or other deferral mechanisms for salvage and/or cost of removal, and regulator's responses to such arguments. The proceedings discussed are ones I have encountered or heard about. Water utilities and telecommunications companies are not represented, because of my limited exposure to such entities. Limited access to the testimony for some of the proceedings discussed required discerning the arguments in favor of deferral from the rebuttal testimony. For the most part, the parties in the proceedings were represented by consultants.

The near-term revenue requirement impact makes cash treatment and other forms of salvage and cost of removal deferral attractive to regulators. The proceedings discussed here demonstrate that this attraction is strong enough to prompt some regulators to dictate cash treatment, even though in conflict with Uniform Systems of Accounts that specify accrual accounting and unfortunate for customers and the economy of the service territory.

Common deferral mechanisms for power plants are to eliminate contingencies and future cost escalation from site-specific demolition cost estimates, and to adopt NRC generic nuclear decommissioning cost estimates when such estimates are lower than site-specific estimates. With the exception of 1993 Indiana Cause No. 39314, these mechanisms are discussed here only when there are other salvage and cost of removal deferral mechanisms in the proceeding.

A common deferral mechanism for property other than power plants is the use of *past* net salvage, rather that the *average* net salvage that is required for calculating whole life depreciation rates or the *future* net salvage that is required for calculating remaining life depreciation rates. The only discussions of this mechanism here involve proposals to utilize past experience as the basis for stepping toward average or future net salvage or assertions that future economies of scale will cause future cost of removal factors to be lower than past factors.

The FERC and Rural Utilities Service Uniform Systems of Accounts dictate accrual accounting, but the 1976 NARUC electric and gas Uniform Systems of Accounts do not include this requirement. This situation may be perceived to limit how a cash basis proposal can be

responded to. However, the accrual accounting requirement can be implied for any electric utility utilizing the NARUC electric Uniform System of Accounts, because the NARUC announced in 1999 that it would no longer maintain it, and encouraged entities to follow the FERC Uniform Systems of Accounts. The more recent (1996) NARUC water Uniform System of Accounts dictates accrual accounting, and I assume that the 1996 NARUC wastewater Uniform System of Accounts does also.

This discussion demonstrates that proposals to defer salvage and/or cost of removal are not a new phenomenon and persist, even in jurisdictions that have recognized their Uniform Systems of Accounts require accrual accounting. The persistence of deferral proposals is evidence of a regulatory fact-of-life – issues do not stay settled.

Some of the proceedings discussed here include assertions that SFAS 143 and the AICPA SOP on property, plant and equipment accounting dictate that removal costs be deferred. While the FASB recently rejected the SOP, the FASB Staff and the AICPA are currently reviewing the draft of the proposed SOP to identify any specific issues that may be appropriate to address through FASB Staff Positions (FSPs). If this is done, the FSPs may resemble international accounting standards. The May 17, 2004 Committee letter addressed requirements of international standards for asset accounting.

If you are familiar with any of the proceedings discussed here and believe I misinterpreted or left out something, please provide me with your thoughts. If you know of other proceedings that deserve similar treatment, please prepare a discussion and email it to me for inclusion in a future Committee letter.

1977 – Delmarva Power & Light Company, Delaware Docket No. 898

In 1975 Docket No. 818, the Staff eliminated net salvage from the depreciation rates for gas property. The Staff had intended to add recorded negative net salvage to revenue requirements as an expense, but failed to do so. The depreciation rates are remaining life, so this treatment shifts recovery of net salvage to the life of replacement property, which produces a deferral well beyond the deferral inherent in a cash basis.

In Docket No. 898, Delmarva asserts that the Docket No. 818 treatment is contrary to GAAP and to the Delaware Uniform System of Accounts; quoting the NARUC publication, Public Utility Depreciation Practices, and the Wisconsin Commission publication, A Review of Legal and Accounting Problems, to demonstrate the GAAP requirements; and quoting the Uniform System of Accounts definitions of depreciation, service value, net salvage, salvage and cost of removal to demonstrate the Delaware accounting requirements.

The Staff agreed with Delmarva's contention in Docket No. 898, and the Commission authorized the depreciation rates that Delmarva had proposed in Docket No. 818. While not significant to this discussion, it is interesting that the authorized depreciation rates utilized a remaining life limit of 35 years to recognize uncertainties imposed by gas supply.

1980 – Southwestern Electric Power Company (SWEPCO), Arkansas Docket Nos. U-3116 and U-3136

The Staff eliminates net salvage from the Transmission, Distribution and General Plant depreciation rates, and proposes remaining life rates. This treatment shifts the recovery of net salvage to the life of the replacement property.

SWEPCO asserts that this net salvage treatment violates the Arkansas accounting rules and prior regulatory precedence; quotes the Uniform System of Accounts definitions of depreciation, service value, net salvage, salvage and cost of removal to demonstrate the Arkansas accounting requirements; refers to its own depreciation rates to demonstrate the regulatory precedence; quotes Public Utility Depreciation Practices to explain the reasons for these rules and precedence; and demonstrates the detrimental impact of the Staff approach on customers.

The Commission adopted the Staff rates, but I understand that successor Staff has gone back to accrual accounting.

1986 – Niagara Mohawk Power Corporation, New York Case Nos. 29327 and 29328

An intervener proposes to defer the cost of removal for new additions. The deferral mechanism is not clear from the rebuttal testimony, but I believe that it is through adopting sinking fund depreciation for cost of removal.

Niagara Mohawk asserts that this deferral shifts recovery to late in life, when productivity has deteriorated and the economic viability of continued operation could be uncertain due to new technology, and requires that life be very accurately estimated; and demonstrates the detrimental impact on customers.

The Commission did not allow the proposed deferral.

1990 – Intermountain Gas Company, Idaho Case No. INT-G-90-1

The Staff proposes that positive net salvage be incorporated into depreciation rates and that negative net salvage be expensed, claiming this treatment is appropriate accounting and appropriate regulation. The Staff relies upon:

> The NARUC publication, Current Issues and Capital Recovery by Telecommunications Utilities, proposing current period accounting;
>
> Public Utility Depreciation Practices commenting that a cash basis for salvage and cost of removal might be more satisfactory than accrual accounting;
>
> An assertion that salvage estimates are not reliable, because they are based on a small number of observations and low retirements relative to balances;
>
> An assertion that Intermountain has no legal obligation for removal, so may choose to abandon and never incur the expense;
>
> An assertion that ratepayers are being asked to finance future expenditures that are the obligation of stockholders; and,
>
> An assertion that if Intermountain is restructured, past negative net salvage collections could be diverted.

Intermountain asserts that the Staff proposes treatment that is not supported by either the NARUC or the accounting profession, and that such treatment is neither appropriate accounting nor appropriate regulation. However, I do not know the details.

In rebuttal, the Staff makes reference to several decisions of other commissions that support the proposed treatment, including FERC decisions that eliminated future cost escalation from removal cost estimates for offshore pipeline facilities and the Penn Sheraton litigation that led to

Pennsylvania requiring that salvage and cost of removal amounts be recorded in the depreciation reserve and amortized to expense over five years.

The Commission continued accrual accounting, but responded to the Staff's reliability assertion by averaging the five-year weighted net salvage percentage experience, reducing the annual percentages to this cap, and recalculating the five five-year average, which decreased Intermountain's proposed depreciation increase for 17% to 14%.

1990 – Missouri Public Service Division (MOPUB), Missouri Case No. ER-90-101

The Staff proposes depreciation rates based on net salvage factors devised to make the annual accrual amounts identical to the annual salvage and cost of removal amounts recorded in the book reserve. The mechanism for doing this is to relate the recorded amounts to the total depreciable investment rather than to the retirement amounts representing the property that caused the salvage and cost of removal.

The Staff initially proposed excluding power plant terminal net salvage, and later proposed that external funding be required if power plant terminal net salvage is recognized. The initial exclusion is particularly significant in view of the Staff's position in the proceeding that recovery of the costs for demolishing three retired power plants not yet removed should be denied. The Staff asserts that power plant land values should be recognized in depreciation, and that the "known and measurable" concept precludes net salvage from being appropriate in power plant depreciation rates.

MOPUB asserts that the appropriate relationship is to the retired property, not to the surviving property; that the Staff approach to net salvage is the equivalent of Retirement Accounting and quotes the Public Utility Depreciation Practices explanation of why accrual accounting long ago replaced Retirement Accounting; that power plant land values cannot be reflected in depreciation rates, because land is not depreciable and depreciation accounting is not a value concept; and that the "known and measurable" concept does not apply to depreciation accounting; quotes the Public Utility Depreciation Practices statement that remaining life depreciation rates require future net salvage; demonstrates the detrimental impact of deferral on customers; and recommends that, if the Commission requires cash treatment for salvage and cost of removal, it be accomplished through true cash accounting, rather than through net salvage factors devised to hide the fact the they are intended to emulate cash accounting.

At the time, the Missouri electric Uniform System of Accounts was that of the NARUC, which did not include an accrual accounting requirement.

The depreciation rates proposed by the Staff were adopted by the Commission.

As is evident from following discussions of 1999, 2001 and 2002 Missouri proceedings in which the Staff adopted true cash accounting, Missouri's later adoption of the 1992 FERC Uniform Systems of Accounts that dictate accrual accounting has not precluded Missouri from continuing a cash basis for net salvage. It is my understanding that the Staff proposed that the FERC requirement for accrual accounting be deleted for Missouri purposes, but the Commission opted to not do so at the time the 1992 FERC electric and gas Uniform Systems of Accounts were adopted. However, the 1999, 2001 and 2002 proceedings not mentioning this requirement makes me wonder if I am incorrect, and that the accrual accounting requirement was stripped out upon adoption.

1991 – Public Service Electric & Gas Company (PSE&G), New Jersey Docket Nos. EE91081428 (electric) and EE91081429 (gas)

An intervener proposes Transmission, Distribution and General Plant depreciation rates based on net salvage factors equivalent to a cash basis. The proposed net salvage factors reflect a cash basis for about one-third of the accounts and three times that amount for the remainder.

The intervener also proposes that future cost escalation be eliminated from the site-specific demolition cost estimates for steam generating units and gas production and storage sites.

PSE&G asserts that a cash basis cannot be used in New Jersey, because General Instruction 11 of the electric and gas Uniform Systems of Accounts dictate accrual accounting; discusses the detrimental impact of depreciation deferral on customers; quotes the page 24 and page 224 Public Utility Depreciation Practices discussions of why net salvage should be reflected in depreciation rates; and refers to the Public Utility Depreciation Practices statement that remaining life depreciation rates require future net salvage.

The Administrative Law Judge adopted the intervener's position on future cost escalation, and concluded that a cash basis violates the New Jersey Uniform Systems of Accounts, so cannot be used. The cases were settled based on an increase for Steam Production Plant and a decrease for Gas Distribution Plant, and on an accrual basis for net salvage.

1993 – Atlanta Gas Light Company (AGL), Georgia Docket No. 4451-U

The Staff faults the AGL net salvage factors for accruing more annual net salvage amounts than are currently being recorded. However, this situation served to support less negative net salvage factors for three accounts, rather than factors reflecting a cash basis.

AGL assertes that this situation is inherent in the accrual accounting requirement of the Commission, and that the Staff is actually arguing against the concept of accrual accounting. AGL addressed the short-term and long-term implications of lower depreciation rates, but did not demonstrate the situation.

The Commission adopted the depreciation rates of the Staff, but provided no rational for its decision.

1993 – Indiana Michigan Power Company, Indiana Cause No. 39314

An intervener attacks the validity of site-specific fossil plant demolition cost estimates. The witness did not address the cost escalation aspect of the cost estimates, but the intervener did in its briefs.

Indiana Michigan responds by questioning the witness' qualifications to address such estimates.

The Commission concluded that the witness is not qualified, so adopted the Indiana Michigan site-specific estimates measured at the price level expected at the time of demolition, and criticized the intervener for its briefs addressing evidence not in the record.

1994 – Delmarva Power & Light Company, Delaware Docket No. 94-22

The Staff and an intervener object to small steps taken for five property groups toward the future cost of removal factors indicated by past experience.

The case was settled without the small steps prior to Delmarva filing rebuttal testimony.

1995 – Delmarva Power & Light Company, Delaware Docket No. 95-224

The Staff proposes cash accounting for electric Transmission, Distribution and General Plant salvage and cost of removal when net salvage is negative, and asks that the Commission open a generic proceeding to address this issue. The 1996 Exposure Draft of what eventually became SFAS 143 is cited in support of the cash accounting proposal. The Staff proposed two sets of depreciation rates, one reflecting net salvage factors on an accrual basis and one reflecting zero net salvage for property groups experiencing negative net salvage. It was unclear which set of rates was actually being recommended.

Delmarva asserts that the Staff's cash basis proposal is incomplete, because the recorded net salvage expense is ignored; that cash accounting is adverse to the long-term interests of customers; that the short-term revenue requirement impact reverses within seven or eight years; that a generic proceeding is not needed, because the Commission had previously concluded in Docket No. 898 that its Uniform System of Accounts dictates accrual accounting; and that the Uniform System of Accounts is now even more specific about accrual accounting, as General Instruction 11 specifying accrual accounting was added since the prior decision; and quotes the page 24 Public Utility Depreciation Practices discussion and earlier discussions of the NARUC and the Staff of the Wisconsin Public Service Commission as to why net salvage should be reflected in depreciation rates.

The case was settled on an accrual basis.

1996 – Public Service Company of Oklahoma (PSO), Oklahoma Cause No. PUD 960000214

The Staff asserts that cost of removal should be recorded in the accumulated provision for depreciation only when property is removed without replacement and should be recorded as a cost of the new property when property is removed with replacement. However, the Staff did not propose depreciation rates based on this assertion.

An intervener proposes that the Commission consider requiring a cash basis for salvage and cost of removal, but did not propose depreciation rates reflecting this proposal.

The Staff and another intervener assert that increased retirement activity in the future will make removal more efficient, thereby decreasing future cost of removal factors.

The Staff faults the inclusion of future cost escalation in an estimate of terminal power plant demolition costs that PSO's proposed terminal net salvage factors stepped toward, asserting that the Uniform System of Accounts does not require future inflation to be reflected in depreciation rates; and faults PSO for not considering the value of land as an offset to demolition costs.

PSO responds to the Staff assertion concerning recording cost of removal by quoting a portion of the Uniform System of Accounts description of Account 108, Accumulated Provision for Depreciation of Electric Utility Plant, and Plant Instructions 11(A), 10(B)(2) and 10(F), and by noting that the list of Components of Construction Cost contained in the Plant Instructions makes

no reference, either implicit or explicit, to removal costs. Plant Instruction 10(B)(2) is particularly significant, and states:

> When a retirement unit is retired from electric plant, with or without replacement, the book cost thereof shall be credited to the electric plant account in which it is included, determined in the manner set forth in Paragraph D, below. If the retirement unit is of a depreciable class, the book cost of the unit retired and credited to electric plant shall be charged to the accumulated provision for depreciation applicable to such property. The cost of removal and salvage shall be charged or credited, as appropriate, to such depreciation account.

PSO asserts that the Uniform System of Accounts does not distinguish between property replaced and property not replaced and that all cost of removal is required to be recorded in the reserve, and demonstrates the detrimental impact of deferring cost of removal on customers.

PSO responds to the proposal to consider a cash basis for salvage and cost of removal by noting that General Instruction 11 of the Uniform System of Accounts dictates accrual accounting, so a cash basis cannot be utilized in Oklahoma.

PSO responds to the assertion concerning the impact of increased retirement activity in the future by demonstrating that the retirement dispersion patterns for the property are too flat to allow room for further economies of scale to be realized, and asserts that any realized economies of scale will be more than offset by future cost escalation.

PSO quotes the Uniform System of Accounts definition of cost of removal to demonstrate that it says nothing about such costs being measured on any basis other than the costs incurred and asserts that neither does any other aspect of the Uniform System of Accounts; asserts that the AICPA (GAAP) definition of depreciation accounting states that depreciation "is a process of allocation, not of valuation," so land values are precluded from being reflected in depreciation; and asserts that the Uniform System of Accounts does not allow gains or losses from the sale of non-depreciable assets, such as land, to be recorded as salvage.

The case was settled on an accrual basis for salvage and cost of removal, and on terminal power plant net salvage factors identical to those proposed by PSO for 18 property groups and more negative than the existing factors but less negative than proposed by PSO for five property groups.

1998 – Georgia Power Company (GPC), Georgia Docket No. 9355-U

The Staff proposes a cash basis for Transmission, Distribution and General Plant net salvage, and that power plant terminal net salvage not be allowed until the retirement decision has been made and the dismantling cost estimate has been prepared. An intervener proposes a cash basis for Transmission and Distribution Plant net salvage. Both the Staff and the intervener propose that site value be reflected in power plant depreciation rates.

GPC asserts that a cash basis cannot be used for net salvage in Georgia, because General Instruction 11 of the Uniform System of Accounts dictates accrual accounting; that the deferral of power plant terminal net salvage until very late in life or beyond the end of life produces a serious intergenerational equity problem; that the AICPA (GAAP) definition of depreciation accounting states that depreciation "is a process of allocation, not of valuation," so land values are precluded from being reflected in depreciation; and that the Uniform System of Accounts does not allow gains or losses from the sale of non-depreciable assets, such as land, to be recorded as salvage.

The depreciation issue was settled by retaining the existing depreciation rates, which reflect a cash basis proposed by the Staff in a 1991 proceeding.

1999 – Laclede Gas Company, Missouri Case No. GR-99-315

This discussion relies upon Laclede's March 29, 2004 filing in response to a Missouri order directing such a filing as a consequence of a remand of the Western District Court of Appeals instructing the Commission "to provide clearer, more detailed findings of fact that include the rationale for the findings." This remand was the result of an appeal of the Commission's second order in the proceeding that was in response to a prior remand by the Circuit Court of Cole County with instructions to provide findings of fact "sufficient to support a resolution of net salvage issues." The issue is findings sufficient to explain why the Commission adopted the Staff's approach to net salvage.

The Staff proposes cash treatment of net salvage and asserts that net salvage should recover the current net salvage, not the average over the life; that Laclede's customers should pay an amount equal to, or nearly equal to, the amount currently being spent; that Laclede has been recovering more than it is spending; that final costs are unmeasurable and unknown except in specific cases; that its method would address an intergenerational equity problem; and that its method is appropriate, since future rate cases will allow adjustments where necessary.

Laclede proposes accrual treatment of net salvage and asserts that its method is consistent with the fundamental goal of depreciation accounting to allocate the full cost over service life so that customers are charged in proportion to the benefit received; and asserts that this goal and Laclede's method for achieving it are supported by the overwhelming weight of authority on how to establish proper depreciation rates; that the method is supported by the definition of depreciation accounting utilized by the NARUC and by GAAP; that the method is consistent with authoritative texts, including that of the NARUC; that the method is almost universally accepted by other state and federal regulatory bodies in the US; that the Staff witness agreed with the premise that negative net salvage should be collected from customers and with the allocation goal; that for new categories of plant or equipment, the Staff approach would provide no net salvage allowance until the facilities are actually retired; that the Staff approach would diminish intergenerational equity by assuring that customers only pay for the net salvage associated with plant no longer used to serve them; and that the same techniques used to estimate net salvage are also used to estimate the service lives of the assets to which the net salvage applies, and that these lives are used to defer the recovery of current capital expenditures.

Laclede's position expressed in its filing is:

> ...That this repeated failure to render adequate findings of fact is not due to some inherent inability on the part of the Commission to summarize the evidentiary record and explain how it supports the Commission's decision to adopt Staff's method. Instead, it derives from the simple fact that there is no competent and substantive evidence on the record of Case No. GR-99-315 to support the Commission's initial decision on this issue.
>
> In view of this consideration, Laclede respectively urges the Commission to issue findings on this occasion that are consistent with the only result that can be supported by the evidentiary record in this case, namely a result that retains the traditional method.

While I have not seen it, I understand that Laclede filed a motion for reconsideration, an application for rehearing and an alternative recommendation for a generic proceeding.

The Commission has decided to reopen the proceeding to take further evidence on depreciation and net salvage, and the proceeding is in progress.

2000 – Central Power & Light Company (CPL), Texas PUC Docket No. 22352, and West Texas Utilities Company (WTU), Texas Docket No. 22354

The two proceedings are for unbundling, so did not involve power plants. The proceedings are separate, but are discussed together because they involved sister organizations, the same witnesses, and the same salvage and cost of removal issues.

An intervener asserts that the cost of removal for property that is replaced is to be recorded on a cash basis and that Electric Plant Instruction 2(D) addressing how contributions are to be recorded supports this assertion, but did not propose depreciation rates based on this assertion; and asserts that increased retirement activity in the future will make removal more efficient, thereby decreasing future cost of removal factors, referring to the 1996 version of Public Utility Depreciation Practices in support of the expectation of future economies of scale.

CPL and WTU quote Electric Plant Instructions 2(D) and 10(B)(2) in support of their assertion that the Uniform System of Accounts does not distinguish between replacements and retirements without replacements; demonstrate that the retirement dispersion patterns for the property are too flat to allow room for further economies of scale to be realized, and that any realized economies of scale will be more than offset by future cost escalation; assert that Transmission Plant retirements tend to be for large projects that further reduce, and probably eliminate, potential economies of scale that will reduce future cost of removal factors; assert that small line crews tend to work more efficiently than do large crews, which makes it unlikely that future economies of scale will reduce future cost of removal factors for Distribution Plant; assert that load growth tends to keep the age of retirements from increasing to an age equal to the average service life, so it is unlikely that the age of any property will increase enough for economies of scale to be realized; and quote the portion of my 1998 SDP Journal article, *Public Utility Depreciation Practices - 1996 Edition*, that indicates my disappointment with its Chapter XI, Estimating Salvage and Cost of removal, to which the intervener makes reference.

CPL and WTU introduced new depreciation studies, but did not propose changing the existing depreciation rates, which are based on accrual of net salvage. The proceedings were settled based on retaining the existing depreciation rates.

2001 – Empire District Electric Company, Missouri Case No. ER-2001-299

This discussion relies upon the September 20, 2001 Commission order.

The order states that the Staff eliminated net salvage from depreciation, indicating that the Staff's approach is true cash accounting. The Commission adopted the Staff position on net salvage, stating:

> Inclusion of net salvage value creates the need to project the date that plant will be removed, the cost of removal at the time it is removed and the gross salvage value, for plant that may never be removed or at least not be removed for some considerable time after it is retired...This uncertainty provides sufficient grounds to reject Empire's determination of net salvage cost. The Staff's approach of

treating net salvage as an expense based on Empire's recent historical data reduces this uncertainty. Additionally, separately stating net salvage cost, rather then incorporating it in depreciation rates, appropriately identifies the significance of net salvage on rates.

2001 – Public Service Electric & Gas Company (PSE&G), New Jersey Docket Nos. GR01050297 and GR01050328

An intervener asserts that PSE&G's depreciation is excessive and that the U. S. Supreme Court in *Lindheimer v. Illinois Bell Telephone Company* states the utility has the burden of showing that depreciation has not been excessive and that predictions must meet the test of experience; that customers suffer from increased depreciation, because depreciation expense flows dollar-for-dollar into revenue requirements; that PSE&G's net salvage proposals are beyond the bounds of rationality and reasonableness, because they are an attempt to recover inflated future removal costs that for the most part will not be incurred and produce a need to consider a better approach to net salvage recovery; that PSE&G had already removed a majority of the gas production and storage facilities related to a 1989 dismantlement cost estimate, so the estimate does not relate to the current facilities; that the net salvage accruals PSE&G proposes for mains and services are unreasonable, because they are more than ten times the actual experience and are more negative than the PSE&G witness proposed in three other proceedings; that the majority of the cost of removal will not be incurred, because plastic mains and services are either replaced next to or inserted into the existing metallic pipe; that the metal mains and services are left in place to allow locating with magnetic devices; that for insertion the existing pipe remains in service, so should not be retired, and the entire replacement effort is for the new pipe, and not for removal of the old pipe; that PSE&G's implication of a link between life and net salvage is wrong; that net salvage should be eliminated from depreciation and the experienced net salvage should be added to depreciation expense, which would provide full recovery; and that Kentucky has adopted this approach for Jackson Energy Cooperative.

PSE&G recognizes that different people can reach different depreciation conclusions, but is astounded by the intervener's one-sidedness demonstrated by every change to PSE&G's proposed depreciation rates being a decrease; asserts that the intervener's proposed depreciation rates are so far below the existing approved rates that they are blatantly unreasonable, and demonstrates that they are among the lowest, if not the lowest, for a gas distribution company in the United States, and would produce a drain on cash flow that would severely hamper PSE&G's ability to internally fund infrastructure improvements and ongoing capital projects; quotes from page 18 of the 1996 version of Public Utility Depreciation Practices to demonstrate that regulatory accounting specifies that cost of removal be incorporated into depreciation rates on an accrual basis, and provides examples; and asserts that departing from the accrual accounting basis reflected in its existing depreciation rates is unfair to customers, quoting from page 33 of the 1968 version of Public Utility Depreciation Practices about the short-run and long-run impact of lower depreciation rates on customers. (Although the wording is not identical, this discussion of the impact on customers is also on page 23 of the 1996 version of the NARUC text.)

PSE&G asserts that *Lindheimer v. Illinois Bell Telephone Company* relates to past depreciation accumulations, not to prospective revisions, that there is no reference to net salvage, and that PSE&G's past accumulations are not excessive, because they are predicated on application of Board authorized depreciation rates; that the intervener's remaining life rate calculation formula is incorrect, because according to Public Utility Depreciation Practices, the correct formula includes a component for future net salvage; that capital recovery shortfall produces intergenerational customer inequity and has the potential for creating stranded assets; that cash treatment conflicts

with the accrual accounting requirement of the New Jersey Uniform System of Accounts; that New Jersey has had a practice of including net salvage in depreciation accruals; that in the 1991 PSE&G cases the ALJ concluded that the proposed cash basis violates the Uniform System of Accounts, so cannot be utilized in New Jersey, and the Board agreed; that the intervener fails to properly recognize that one goal of depreciation is to allocate costs over life and the cause and effect relationship between the retirement (cause) and the cost of removal (effect); that actual experience validates the production and storage dismantlement estimates; and that the intervener refuses to acknowledge that the remaining production and storage facilities will need to be dismantled; and demonstrates the shortfall of capital recovery that would result from the intervener's cash basis for net salvage be calculating a 30% book reserve shortfall for mains in five years and a negative reserve in 29 years.

I do not have the PSE&G testimony that rebutted the intervener's position on the significance of pipe replacement practices to life and net salvage.

The case was settled by retaining the existing depreciation rates that reflect accrual accounting.

2002 – AmerenUE (UE), Missouri Case No. EC-2002-1

The Staff proposes true cash accounting for net salvage, asserting that the definition of depreciation in Public Utility Depreciation Practices indicates that only capital costs are to be reflected in depreciation rates; that net salvage costs that may occur far in the future should not be collected from customers until they occur; and that the 1962 Penn Sheraton court order supports expensing of net salvage.

UE asserts that the Public Utility Depreciation Practices depreciation definition is the same as in the Uniform System of Accounts, which specifies that depreciation is loss in service value, thereby incorporating net salvage in depreciation; that the UE witness knows of no authoritative text on depreciation that supports the Staff position on net salvage; that Public Utility Depreciation Practices and Depreciation Systems support incorporating cost of removal in depreciation; that cost of removal relates to the plant rendering service, so would be allocated over the life of the plant; that deferral increases the present value of revenue requirements, referring to a 1992 paper presented to the AGA and EEI; that there should be no concern for net salvage accruals currently exceeding recorded net salvage, as it is due to growth and maturity; that, if there is concern, plant additions should be expensed; that the sensitivity of net salvage factors to the age of retirements means that net salvage costs will increase in the future; that there is no less certainty about net salvage estimates than about life estimates; that the Penn Sheraton case stems from an era when fair value determined rate base, precluded depreciation expenses from being based on fair value, was inappropriately applied to prospective net salvage, and continues net salvage as a capital cost; that the Staff position is inconsistent with the Commission's decision in St. Louis Water Case No. WR-2000-844 to reflect net salvage on an accrual basis; that UE needs the cash flow from accrual of net salvage; that incorporating net salvage in depreciation rates is equitable and sound ratemaking; and that expensing net salvage is not equitable and violates the principle that customers pay the cost of the plant that provides service to them; and demonstrates the inequity.

The case was settled for a dollar amount depreciation decrease, so the Commission did not address the net salvage treatment.

2002 – Hawaiian Electric Company (HECO), Hawaii Docket No. 02-0391

An intervener addresses SFAS 143, FERC Order No. 631 and the AICPA SOP on property, plant and equipment accounting, but sometimes referred to them as involving net salvage and sometimes referred to them as involving cost of removal. The intervener asserts that the determination of non-production plant net salvage is problematical, because retirements are valued at original cost while net salvage is valued at current cost, and proposes two alternatives for handling net salvage.

One alternative is adoption of the liability accounting for asset retirement obligations (AROs) specified by SFAS 143 and is stated to reflect the intervener's interpretation of FERC Order No. 631 adopting the SFAS 143 ARO treatment for regulatory accounting purposes. The intervener deducted his estimate of the net salvage amount claimed to be currently recorded in HECO's book reserve, and ended up with a quite small amount of annual accretion expense. The intervener utilized the theoretical reserve approach to estimate the current reserve amount, and recommended an annual negative net salvage amount about 4% of what he asserted is HECO's proposal. In supplemental testimony, the intervener modified this alternative to cover only a single power plant, for which he asserts HECO has a legal ARO.

The other alternative is to utilize what the intervener refers to as the Pennsylvania approach, based on the average of the most recent five years of recorded net salvage, implemented through net salvage factors devised to produce annual depreciation accrual amounts identical to the annual net salvage amounts recorded in the book reserve. (This is actually different from the Pennsylvania approach, as Pennsylvania amortizes to expense over five years the net salvage recorded in the book reserve, which is a bit more deferred than the intervener's proposal.) The intervener asserts that HECO would be assured full recovery; that customers should not be required to pay for estimated future inflation; that the approach is simple and easy to implement; and that the approach conforms to FERC Order No. 631. The intervener recommends an annual negative net salvage amount identical to the recorded amount, which is about 14% of what he asserts is HECO's proposal. In supplemental testimony, the intervener faults HECO for referring to this alternative as a cash basis.

The intervener asserts that the National Study of Unit Retirements of the firm of its witness can be used to judge the reasonableness of power plant dismantlement assumptions; that there is a low probability of HECO or anyone else incurring power plant demolition costs; that HECO's proposed depreciation rates reflect "greenfield" assumptions; that the very low probability of plant dismantlement by HECO means net salvage should be excluded from depreciation rates; and that under GAAP, HECO will not be allowed to capitalize dismantlement costs.

HECO asserts that price level changes over time should be reflected in depreciation, quoting the FERC Uniform System of Accounts as stating that a utility will maintain records that will reflect the percentage of salvage and cost of removal for retired property, and responds to the first alternative by quoting from that portion of FERC Order No. 631 that states it does not change the treatment of non-ARO cost of removal. HECO faults the intervener's present value calculations for utilizing net salvage factors that are inconsistent with SFAS 143 and FERC Order No. 631, and asserts that depreciation accounting is a cost allocation process – not a process of valuation.

HECO quotes from page 18 of the 1996 version of Public Utility Depreciation Practices to demonstrate that regulatory accounting specifies that cost of removal be incorporated into depreciation rates on an accrual basis, and asserts that accrual accounting is required by GAAP. While HECO utilizes the NARUC electric Uniform System of Accounts, HECO asserts that cash accounting violates it, noting that the NARUC no longer maintains its electric Uniform System of Accounts and has encouraged entities to follow the FERC Uniform System of Accounts, which

dictates accrual accounting. HECO asserts that departing from the accrual accounting basis reflected in its existing depreciation rates is unfair to customers, quoting from page 33 of the 1968 version of Public Utility Depreciation Practices about the short-run and long-run impact of lower depreciation rates on customers.

The HECO rebuttal testimony discusses the disposition of the following proceedings in which the intervener's consultant proposed depreciation rates based of the cash basis:

> Midwest Energy, Kansas Case No. 02-MDWG-922-RTS – the Commission adopted accrual accounting.
>
> Elizabethtown Gas Company, New Jersey Docket No. GR02040245 – the Board retained the existing depreciation rates.
>
> Public Service Electric & Gas Company, New Jersey Docket No. ER02050303 – the Board retained the existing depreciation rates.
>
> Jersey Central Power & Light Company, New Jersey Docket No. ER02080506 – the Board adopted the consultant's proposal.
>
> Rockland Electric Company, New Jersey Docket No. ER02080614 – the Board adopted the consultant's level of excess reserve, which reflected a different net salvage level. I understand that the adopted depreciation rates reflect net salvage factors devised to produce annual depreciation accrual amounts identical to the annual net salvage amounts recorded in the book reserve.
>
> Sierra Pacific Power Company, Nevada Docket No. 02-11031 – the Commission adopted Sierra Pacific's net salvage factors based on accrual accounting for all but one of the Transmission and Distribution plant accounts.

I understand that the above Public Service Electric & Gas Company proceeding is the 2001 proceeding discussed earlier. With the exception of that proceeding, I have no knowledge of the arguments for and against a cash basis in these proceedings.

HECO asserts that is has no legal AROs; that the intervener's generating unit retirement study actually demonstrates that there is substantially more than a low probability that any particular plant or unit might be demolished; that the locations of HECO's power plants will likely generate public pressure for removal; that limited space for locating Hawaiian power plants makes it probable that existing units will have to be removed so sites can be reused; that the demolition cost estimates used by HECO reflect various assumptions about the extent of demolition; and that HECO has never capitalized dismantlement costs.

The case was settled based on accrual treatment of net salvage through depreciation.

2003 - PSI Energy, Indiana Cause No. 42359

The Staff concludes that the depreciation increase proposed by PSI is not due to changes in study methods, and recommends that the proposed rates be approved.

An intervener asserts that including future net salvage and terminal net salvage in depreciation rates is unreasonable, because they increase rates for inflated estimates of costs that probably will not be incurred; that PSI's depreciation is excessive and that the U. S. Supreme Court in *Lindheimer v. Illinois Bell Telephone Company* states the utility has the burden of showing that depreciation has not been excessive and that predictions must meet the test of experience; that the National Study of Unit Retirements of the firm of its witness can be used to judge the

reasonableness of power plant dismantlement assumptions; that including negative net salvage in depreciation rates is the equivalent of capitalizing or adding the estimated cost of removal to the original cost of the asset; that the proper way to reflect net salvage in depreciation rates is at present value; that use of a group life and charging removal costs and the original cost of a retired asset to the accumulated depreciation reserve make utility depreciation accounting unique; that depreciation expense flows dollar-for-dollar into revenue requirements, so excessive depreciation expense results in an excessive revenue requirement; that PSI capitalized costs for which there is no legal obligation to incur and then inflated the costs, so current ratepayers will pay for future inflation of costs that will not be incurred; that the site-specific power plant demolition cost estimates are inflated; that it is doubtful that PSI will ever dismantle any of the power plants to "greenfield" conditions and PSI has no current plans to retire the plants; that PSI has no legal obligation to dismantle the plants, so it is unreasonable to assume dismantlement; that removal costs will be part of the cost of a new plant, if plant sites are reused; that past practice suggests PSI will not dismantle retired power plants; that dismantlement estimates should be excluded in their entirety in view of the very low probability of actual dismantlement; that the 1996 version of Public Utility Depreciation Practices states some regulators are requiring salvage and/or cost of removal be expensed when incurred; and that the FERC requires segregation of legal and non-legal AROs and segregation of non-legal AROs for depreciation purposes.

The intervener proposes two alternatives for handling net salvage. One alternative is adoption of the liability accounting for AROs specified by SFAS 143. The intervener deducted PSI's estimate of the net salvage amount currently recorded in its book reserve, and ended up with a quite small amount of annual accretion expense. The intervener recommended an annual negative net salvage amount about 6% of what he asserts is PSI's proposal.

The other alternative is to utilize what the intervener refers to as the Pennsylvania approach, based on the average of the most recent five years of recorded net salvage, implemented through net salvage factors devised to produce annual depreciation accrual amounts identical to the annual net salvage amounts recorded in the book reserve. The intervener asserts that PSI would be assured full recovery; that customers should not be required to pay for estimated future inflation; that the approach is simple and easy to implement; and that the approach conforms to FERC Order No. 631. The intervener recommended an annual negative net salvage amount identical to the recorded amount, which is about 13% of what he asserts is PSI's proposal. The intervener indicates a preference for this approach, and references two New Jersey decisions (Rockland Electric Company and Jersey Central Power & Light Company), two Missouri decisions (Empire District Electric Company and Laclede Gas Company), and two Kentucky decisions (Fleming-Mason Cooperative and Jackson Energy Cooperative) in which this approach was adopted.

Another intervener proposes cash treatment for Transmission, Distribution and General Plant net salvage, and power plant dismantlement costs based on the current price level and excluding contingencies.

The PSI depreciation witness knows of no authoritative text on depreciation that supports the intervener's position on net salvage, and asserts that Public Utility Depreciation Practices and Depreciation Systems support incorporating cost of removal in depreciation; that cost of removal relates to the plant rendering service, so should be allocated over the life of the plant; that it is not appropriate to reflect only current net salvage costs, because current costs are related to plant that previously rendered service; that deferral increases the present value of revenue requirements; that expensing net salvage results in increasing the revenue requirements over the life of the plant; that there should be no concern for net salvage accruals currently exceeding recorded net salvage, as it is due to growth; that, if net salvage accruals should be limited to current cost, why

should not the depreciation expense related to original cost be increased to the current level of plant additions; that the sensitivity of net salvage factors to the age of retirements means that net salvage costs will increase in the future; that Missouri approaches net salvage treatment case-by-case and in St. Louis Water Case No. WR-2000-844 adopted net salvage on an accrual basis; that the Kentucky decisions involve small cooperatives that do not maintain salvage and cost of removal records by account; that 47 states use the traditional treatment of net salvage through depreciation; that Indiana has allowed PSI to use the traditional approach for many decades; that SFAS 143 and FERC Order No. 631 do not apply to the PSI proceeding in Indiana; that customers today paying for future cost of removal and receiving a return on such payments is no different from the utility recovering today amounts invested many years ago and receiving a return in the meantime; that power plant dismantlement based on current cost will result in under-recovery and customer inequity; that inflation of power plant demolition costs will continue; that future changes to power plant demolition technology will not decrease future costs to the current cost level; that PSI's power plant demolition costs reflect a 17% decrease for future efficiencies; that an assumption that power plants will not be dismantled does not recognize the value of the real estate upon which they are located, PSI's commitment to the communities it serves, and the difficulty in obtaining new sites; that incorporating net salvage in depreciation rates is equitable and a sound ratemaking principle, and conforms to the definition of depreciation as the loss in service value; that costs should be collected from the customers that receive service; and that expensing net salvage is not equitable and violates the principle that customers pay the cost of the plant that provides service to them; and demonstrates the inequity.

Other PSI witnesses describe the purpose of cost estimate contingencies as being for the unknowns that experience demonstrates will occur on complex projects, such as power plant demolition; and assert that the cost estimates do not assume "greenfield" conditions, and provide estimates of the cost increases that would occur if "greenfield" conditions were assumed; that the only PSI boilers currently retired in place are for recently repowered units for which continued operation precludes demolition from being cost effective; and that the existing generating units will be demolished in order to reuse the sites; and describe PSI's experience in power plant demolition and site reuse.

The Commission recognized that evaluation of depreciation expenses involves examination of many variables, that *Lindheimer v. Illinois Bell Telephone Company* identified uncertainties associated with the use of depreciation expenses, and that excess depreciation is ultimately passed on to ratepayers, and concluded:

> PSI's power plant demolition cost estimates do not assume a return to "greenfield" conditions; the boilers currently retired in place do not indicate that existing plants will not be demolished at the end of their useful lives; dismantling cost estimates should recognize contingencies; and not including inflation in cost estimates flies in the face of matching rates with costs incurred for service – a sound ratemaking principle followed by the Commission.
>
> Passing dismantlement costs on to a future generation of customers is not sound regulatory policy and is not based on sound ratemaking principles, so such costs should be included in the depreciation rates.
>
> Pennsylvania follows a directive of the Pennsylvania Supreme Court for treatment of net salvage, subsequent decisions in Missouri and Kentucky have been on an accrual basis, and there is a sound basis for the traditional approach utilized by the majority of states.

Historical net salvage (the cash basis) does not take into account the current system configuration or the significantly enhanced customer base, so must be rejected.

The depreciation rates proposed by PSI should be authorized.

2003 – Southern California Edison Company (SCE), California Docket No. A.02-05-004

The PUC Office of Ratepayer Advocates (ORA) expresses concern for increasing cost of removal factors, and proposes several alternative responses:

Do not allow the existing net salvage factors to be changed and require SCE to address the situation in its next general rate case;

Consider a cash basis or sinking fund for net salvage, referring to the 1996 version of Public Utility Depreciation Practices as indicating that regulators are abandoning the treatment of salvage and cost of removal through depreciation accounting; or,

Initiate an Order Initiating Investigation.

ORA asserts that depreciation does not affect the ability to provide safe and reliable service, and that shareholders will still recover their investments in plant over time, if depreciation rates are reduced, and recommends that depreciation rates not be allowed to change.

An intervener asserts that the FERC electric Uniform System of Accounts specifies that cost of removal is to be recorded in the accumulated provision for depreciation when property is removed without replacement and is to be recorded as a cost of the new property when property is removed with replacement. This assertion is supported by the following Uniform System of Accounts definition quoted in testimony and by a site preparation cost example in response to a Data Request.

Replacing or replacement, when not otherwise indicated in the context, means the construction or installation of electric plant in place of property retired, together with the removal of the property retired.

The intervener did not propose depreciation rates that reflect this assertion.

The intervener asserts that cost of removal factors will decrease in the future, as greater numbers of items will be removed; that a power plant site is so valuable that terminal net salvage is positive, as selling the plant is more probable than operating to the end of its life and decommissioning it; and that the offering price of an office park near SCE's General Office indicates 50% net salvage is appropriate for SCE's general purpose buildings.

SCE asserts that ORA's net salvage proposals conflict with PUC policy as reflected in its Standard Practice U-4; that General Instruction 11 of the Uniform System of Accounts dictates accrual accounting; that sinking fund requires very accurate estimates of life, salvage and cost of removal, which is one of the reasons the 1996 version of Public Utility Depreciation Practices gives for sinking fund being rarely used today; that a cash basis and sinking fund conflict with GAAP and would result in misleading financial statements; that deferral creates an intergenerational equity problem and is detrimental to customers; and that the claimed trend to cash treatment of salvage and cost of removal does not exist; describes the significance of the sensitivity of salvage and cost of removal factors to the age of retired property, and presents an analysis showing that cost of removal increases are consistent with increases in construction costs, a finding consistent with SCE's contention that cost of removal factor increases are due to

increased labor rates; demonstrates the detrimental impact of depreciation decreases on customers; and quotes the portion of my 1998 SDP Journal article, *Public Utility Depreciation Practices - 1996 Edition*, that indicates my disappointment with its Chapter XI, Estimating Salvage and Cost of Removal, to which the ORA makes reference.

SCE responds to the assertion concerning the treatment of cost of removal by quoting the Uniform System of Accounts description of Account 108, Accumulated Provision for Depreciation of Electric Utility Plant, and Plant Instructions 11(A), 10(B)(2) and 10(F); asserts that the FERC Uniform System of Accounts does not distinguish between property replaced and property not replaced, and that all cost of removal is required to be recorded in the reserve; and asserts that no utilities follow the treatment claimed by the intervener, providing citations (including California) where regulatory bodies have denied the treatment.

SCE asserts that the intervener's site preparation cost example is not applicable, because the example does not involve the removal of existing facilities, so does not meet the Uniform System of Accounts definition of cost of removal and cannot be recorded as cost of removal, and that when site preparation costs involve existing facilities, removal costs would meet the Uniform System of Accounts definition of cost of removal and would be recorded as cost of removal.

SCE asserts that any expected economies of scale are reflected in its proposed depreciation rates; demonstrates that the retirement dispersion patterns for the property are too flat to allow room for further economies of scale to be realized; and asserts that any realized economies of scale will be more than offset by future cost escalation; that Transmission Plant retirements tend to be on large projects that further reduce, and probably eliminate, potential economies of scale that will reduce future cost of removal factors; that small line crews tend to work more efficiently than do large crews, which makes it unlikely that future economies of scale will reduce cost of removal factors for Distribution Plant; and that load growth tends to keep the age of retirements from increasing to an age equal to the average service life, so it is unlikely that property age will increase enough for further economies of scale to be realized.

SCE asserts that GAAP states that depreciation "is a process of allocation, not of valuation," so site values are precluded from being reflected in depreciation; that the Uniform System of Accounts does not allow gains or losses from the sale of non-depreciable assets, such as land, to be recorded as salvage; that selling prices of power plants are not useful for determining the value of existing equipment, because that portion of the prices applicable to the existing facilities is not disclosed, and quotes a list of ten transaction features that can influence purchase prices from *The Valuation of Industrial Facilities* in the 1998-1999 Issue #4 of The Journal of the International Machinery & Technical Specialties Committee of the American Society of Appraisers; that the market for power plants today is much different from the market at the time its gas-fired generating units were sold to comply with the PUC policy at the time; that it has no plans to sell the plant and is prohibited by the PUC from selling the plant until at least 2006 and there is no assurance that the PUC would allow selling a coal-fired station, and speculates as to why SCE would ever part with a power plant site if it is so valuable; and that the intervener does not know the portions of the office park offering price applicable to the depreciable structures and the non-depreciable land, so has inappropriately assigned the site value to the structures; and describes the appropriate accounting for the sale of a building, utilizing an illustration demonstrating that the intervener's claimed 50% net salvage is really negative 25%.

The proposed decision of the ALJ states that "the extensive exercise of subjective and potentially biased judgment by the respective depreciation experts renders their analyses and recommendations unreliable for purposes of ordering major changes in depreciation parameters

and expenses," and concludes that the existing depreciation rates not be changed. The ALJ states that the intervener's power plant net salvage proposal lacks merit, and mentions the intervener's assertion concerning how cost of removal should be recorded, but does not address it.

The ALJ's concern for the exercise of judgment is inconsistent with SCE testimony that understanding past experience is required to provide assurance that depreciation rates are appropriate for the property under study, that SCE's depreciation study emphasized understanding the significance of the past, and that SCE should be complemented for this emphasis.

The Commission has not yet issued an order.

2003 – South Jersey Gas Company (SJG), New Jersey Docket No. GR03080683

An intervener asserts that including future net salvage and terminal net salvage in depreciation rates is unreasonable, because they increase rates for inflated estimates of costs that probably will not be incurred; that SJG's depreciation is excessive and that the U. S. Supreme Court in *Lindheimer v. Illinois Bell Telephone Company* states the utility has the burden of showing that depreciation has not been excessive and that predictions must meet the test of experience; that the proper way to reflect net salvage in depreciation rates is at present value; that use of a group life and charging removal costs and the original cost of a retired asset to the accumulated depreciation reserve make utility depreciation accounting unique; that depreciation expense flows dollar-for-dollar into revenue requirements, so excessive depreciation expense results in an excessive revenue requirement; that the 1996 version of Public Utility Depreciation Practices states some regulators are requiring salvage and/or cost of removal be expensed when incurred; and that FERC Order No. 631 requires segregation of non-legal AROs for depreciation purposes, and SJG has not done so.

The intervener proposes net salvage factors based on what he refers to as the Pennsylvania approach, based on the average of the most recent five years of recorded net salvage, implemented through net salvage factors devised to produce annual depreciation accrual amounts identical to the annual net salvage amounts recorded in the book reserve. The intervener asserts that SJG would be assured full recovery; that customers should not be required to pay for estimated future inflation; that the approach is simple and easy to implement; that the approach conforms to FERC Order No. 631; and that the proposed treatment does not abandon accrual accounting. The intervener recommended an annual negative net salvage amount identical to the recorded amount, which is about 9% of what he asserts is SJG's proposal. The intervener references two New Jersey decisions (Rockland Electric Company and Jersey Central Power & Light Company), two Missouri decisions (Empire District Electric Company and Laclede Gas Company) and two Kentucky decisions (Fleming-Mason Cooperative and Jackson Energy Cooperative) in which this approach was applied.

The SJG witness knows of no authoritative text on depreciation that supports the intervener's position on net salvage, and asserts that Public Utility Depreciation Practices and Depreciation Systems support incorporating cost of removal in depreciation; that cost of removal relates to the plant rendering service, so should be allocated over the life of the plant; that it is not appropriate to reflect only current net salvage costs, because current costs are related to plant that previously rendered service; that deferral increases the present value of revenue requirements; that expensing net salvage results in increasing the revenue requirements over the life of the plant; that expensing cost of removal when incurred is not accrual accounting; that if net salvage accruals should be limited to current cost, why should not the depreciation expense related to original cost be increased to the current level of plant additions; that the sensitivity of net salvage factors to the

age of retirements means that net salvage costs will increase in the future; that the intervener proposes a radical change that unfairly forces future ratepayers to pay the cost of providing service to current ratepayers; that *Lindheimer v. Illinois Bell Telephone Company* relates to physical deprecation for determining rate base, not to accounting depreciation; that Missouri approaches net salvage treatment case-by-case and in St. Louis Water Case No. WR-2000-844 adopted net salvage on an accrual basis; that the Kentucky decisions involve small cooperatives that do not maintain salvage and cost of removal records by account; that 46 states use the traditional treatment of net salvage through depreciation; that New Jersey's practice is to allow gas distribution companies to include net salvage in depreciation and has allowed SJG to do so; that the Rockland and Jersey Central decisions reflect circumstances unique to electric companies, referring to the Rockland order as stating the net salvage treatment is appropriate "in order to offset the increase [to rates] associated with the deferred balances that were incurred over the 4-year transition period, as well as the increase in Basic Generation Service ("BGS") charges for current service;" that the intervener agreed in responses to Data Requests that neither SFAS 143 nor FERC Order No. 631 are contrary to net salvage being reflected in depreciation rates; that SFAS 143 and FERC Order No. 631 do not apply to ratemaking and violate principles of matching and customer equity; that customers today paying for future cost of removal and receiving a return on such payments is no different from the utility recovering today amounts invested many years ago and receiving a return in the meantime; that incorporating net salvage in depreciation rates is equitable and a sound ratemaking principle, and conforms to the definition of depreciation as the loss in service value; that costs should be collected from the customers that receive service; and that expensing net salvage is not equitable and violates the principle that customers pay the cost of the plant that provides service to them; and demonstrates the inequity.

The ALJ's proposed decision has not yet been issued.

2003 – Consumers Energy Company, Michigan Case No. U-12999

The Staff asserts that cost of removal should be limited to the average of the factors experienced during the last five years, which results in a composite negative net salvage factor of 69%; that the five-year average basis was used in two other Michigan proceedings; that Consumers asks for negative net salvage that exceeds its depreciable plant balance; that Consumers' alternative proposal is nearly as much (92%) as its plant balance; and that Consumers' request is more negative than other Michigan gas utilities.

An intervener faults Consumers for not relating removal costs to construction costs and asserts that Consumers has ignored the net salvage experience for Transmission Plant; that future inflation will be significantly different from past inflation, so the influence of the high inflation rates of the 1970s and 1980s should not be allowed to be reflected in the net salvage factors (the witness' adjustment to eliminate the effect of high inflation rates demonstrates that future retirements will be much older than the retirements reflected in Consumers' net salvage factors, but there is no adjustment for this situation); that depreciation rates should be based on net salvage factors devised to accrue annual net salvage amounts identical to the annual amounts recorded in the book reserve, referring to Georgia, New Jersey and Pennsylvania as using this approach and quoting the 1996 version of Public Utility Depreciation Practices as stating that some commissions are moving away from including net salvage in depreciation rates; that the cost of removal component of the rates should be segregated for accrual purposes; and that traditional methods for calculating depreciation fail to recognize the present value of future costs, resulting in a permanent and growing loan from ratepayers to Consumers, and may be precluded by changes to accounting rules, referring to the SOP that was submitted to and recently rejected

by the FASB. The intervener calculated cost of removal factors based on SFAS 143 treatment, but did not propose that they be reflected in depreciation rates.

Another intervener asserts that Consumers asks for negative net salvage that is seven times larger than is currently being recorded in the book reserve; that Consumers' accrual basis produces intergenerational inequities; that net salvage should be excluded from depreciation and treated as a cash basis; that pages 157 and 158 of the 1996 version of Public Utility Depreciation Practices state that some commissions are moving away from including net salvage in depreciation rates, thereby indicating that excluding net salvage from depreciation is consistent with other jurisdictions and is acceptable to the NARUC; that Pennsylvania excludes net salvage from depreciation rates and the Missouri did so in Empire District Electric Company Case No. ER-2001-299; that if the Commission elects to continue to reflect net salvage in depreciation, future inflation should be excluded from the net salvage factors, which can be accomplished by multiplying the factors proposed by Consumers by 14% – the ratio of the annual recorded amount ($8.3 million) to the annual amount reflected in the proposed factors ($58.4 million); that an account for which the depreciation reserve exceeds the depreciable balance is over-depreciated and should have a zero depreciation rate; and that if Consumers has no legal obligation to retire assets it would not incur any net salvage expense.

Consumers quotes the GAAP definition of depreciation accounting to demonstrate that the cash basis for net salvage of the other parties is inconsistent with fundamental principles applicable to depreciation accounting; asserts that the proposals fail to properly reflect net salvage by using limited, non-representative data, because the parties utilized total company data, not data by accounting function or account, and demonstrates the impact of this skewing; that limiting the data to five years without evaluating its significance magnifies timing mismatches and fails to recognize the impact of non-representative activities; that the proposals allocate costs in a way that results in intergenerational inequity and in net salvage that is not systematic and rational, and involve significant changes from the traditional methodology used to calculate depreciation rates, quoting the 1968 and 1996 versions of Public Utility Depreciation Practices as stating that future net salvage is required to calculate the remaining life depreciation rates proposed by all parties; that a cash basis is inconsistent with the accrual account provision of the Michigan Uniform System of Accounts and with the past practices of the Commission; that the other parties propose depreciation rates that are too low, quoting the 1968 version of Public Utility Depreciation Practices discussion of the adverse effect of such rates on customers; and that adjustments to depreciation rates should be gradual, not abrupt as proposed by the other parties (the other parties propose 35%, 48% and 67% decreases to the existing rates).

Consumers responds to the Staff's contention that negative net salvage exceeding the depreciable plant balance means that the level is too high by quoting the 1996 version of Public Utility Depreciation Practices as stating that net salvage sometimes exceeds the original cost; and by asserting that the comparison with three other utilities is misleading at best, because depreciation parameters are impacted by a wide variety of factors and forces.

Consumers responds to the first intervener by asserting that the intervener is mistaken that Consumers ignored recent removal experience for Transmission Plant; that criticizing the treatment of inflation introduces an element of valuation that is inconsistent with the GAAP statement that depreciation is a cost allocation concept, not a valuation concept; that under the traditional approach the customer pays only his pro rata share of the total cost of an asset over its life that results in a declining revenue requirement; that a growing rate base is irrelevant, because the depreciation expense and return components of revenue requirements are fixed; that the cash basis causes higher future rate base and increased costs for future customers; that sound

engineering judgment is an element of any depreciation study, and that all of Consumers' judgments are based on hard data, not upon speculation; that comparing current removal costs with current construction costs is neither necessary nor useful for a depreciation study; that GAAP and regulatory accounting requirements are improperly intertwined by the intervener and used interchangeably, implying there are no differences when there are differences; that Consumers' gas operation is not subject to FERC jurisdiction, so there is no regulatory accounting rule for segregation of cost of removal; that SFAS 143 and FERC Order No. 631 do not require cash treatment; and that SFAS 143 does not apply to regulatory accounting and does not say anything about non-legal obligations, so the proposed alternative methodology would not be appropriate.

Consumers responds to the other intervener by asserting that the fact that accrued net salvage is greater than recorded net salvage is not significant; that criticizing the treatment of inflation introduces an element of valuation that is inconsistent with the GAAP statement that depreciation is a cost allocation concept, not a valuation concept; that Consumers made no adjustment to reflect future changes in cost; that GAAP and regulatory accounting requirements are improperly intertwined by the intervener and used interchangeably, implying there are no differences when there are differences; that, in addition to being contrary to fundamental principles of depreciation and in conflict with Michigan accounting requirements, the proposal to shift net salvage from depreciation to current expense would eliminate the important self-correction benefit of remaining life depreciation; and that the 1996 version of Public Utility Depreciation Practices does not endorse treating net salvage as a current expense.

The ALJ's proposed decision has not yet been issued.