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Issues:	Depreciation Expense
Witness:	Larry E. Kennedy
Exhibit Type:	Surrebuttal
Sponsoring Party:	Missouri-American Water Company
Case No.:	WR-2020-0344
Date:	February 9, 2021

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WR-2020-0344

SURREBUTTAL TESTIMONY

OF

LARRY E. KENNEDY

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

AFFIDAVIT

I, Larry E. Kennedy, under penalty of perjury, and pursuant to Section 509.030, RSMo, state that I am a Senior Vice President for Concentric Energy Advisors, Inc., that the accompanying testimony has been prepared by me or under my direction and supervision; that if inquiries were made as to the facts in said testimony, I would respond as therein set forth; and that the aforesaid testimony is true and correct to the best of my knowledge and belief.



Larry E. Kennedy

February 9, 2021

Dated

**SURREBUTTAL TESTIMONY
LARRY E. KENNEDY
MISSOURI-AMERICAN WATER COMPANY
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SURREBUTTAL TESTIMONY

LARRY E. KENNEDY

I. INTRODUCTION

1 **Q. Please state your name and business address.**

2 A. My name is Larry E. Kennedy, and my business address is Suite 277, 200 Rivercrest Drive
3 S.E. Calgary Alberta, Canada

4 **Q. Are you the same Larry E. Kennedy who previously submitted direct testimony in**
5 **this proceeding?**

6 A. Yes.

II. OVERVIEW

7
8 **Q. What is the purpose of your Surrebuttal Testimony in this proceeding?**

9 A. The purpose of my Surrebuttal Testimony is to provide responses to the rebuttal
10 testimonies of Missouri Public Service Commission Staff (“Staff”) witness Cedric E.
11 Cunigan, and Office of the Public Counsel (“OPC”) Witness John A. Robinett.

12 **Q. Please provide a summary of the depreciation evidence in this proceeding thus far**

13 A. Missouri-American Water Company (“MAWC” or “Company”) filed my Direct
14 Testimony to provide expert testimony related to the Company’s proposed depreciation
15 rates and associated depreciation expense. My Direct Testimony included a full and
16 comprehensive depreciation study for both the MAWC water and wastewater operations.
17 In response to my Direct Testimony, Commission Staff filed a Cost of Service report
18 (“Staff COS Report”) on November 24, 2020, that included comment on the depreciation

1 study, and in particular on the topic of the use of Amortization Accounting for a number
2 of general plant accounts. Additionally, prior to and following the submission of the Staff
3 Cost of Service Report, MAWC responded to depreciation related Data Requests, seeking
4 clarification on a number of topics related to the depreciation study, including all data files
5 used in the completion of the study. On January 15, 2021, the rebuttal testimonies of
6 Commission Staff witness Cunigan, and OPC witness Robinett were filed.

7 **Q. Did Staff note a difficulty as of the filing of the Staff COS Report?**

8 A. Yes. In the Staff COS Report, the Commission Staff noted:

9 *“Staff is still in the process of reviewing the additional information*
10 *provided by MAWC, and is thus unable to confirm the results of MAWC’s*
11 *depreciation study as of the filing date of this report”¹(emphasis added)*

12 **Q. Was the Company able to resolve Staff’s concern?**

13 A. Yes. In order to assist Commission Staff, a Microsoft Teams meeting was held with the
14 Commission Staff, MWAC staff and Concentric Staff, to provide the procedures required
15 for Commission Staff to upload the Concentric data files into the Commission’s
16 depreciation software.

17 **Q. Thereafter, did Staff have any further concerns regarding the availability of data?**

18 A. No, not to my knowledge.

19 **III. SURREBUTTAL TO THE REBUTTAL TESTIMONY OF MR. CUNIGAN**

20 **Q. Please summarize the Rebuttal Testimony of Mr. Cunigan?**

21 A. The Rebuttal Testimony of Mr. Cunigan indicates that the Staff still has issues with the
22 MAWC use of amortization for certain general plant accounts and with MAWC’s use of

¹ WR-2020-0344 Staff Cost of Service Report, page 47.

1 the 1996 version of the USoA as compared to use of the 1976 version of the USoA.

2 **Q. Was Staff witness Cunigan able to verify MAWC's study results?**

3 A. Yes Mr. Cunigan stated:

4 *Staff reviewed the depreciation study provided in Direct Testimony of*
5 *MAWC witness Larry E. Kennedy. Staff also requested the source data for*
6 *this depreciation study in Staff Data Request No. 0093. **Staff has been able***
7 *to replicate similar results to that of MAWC witness Larry E. Kennedy*
8 *since the filing of the Staff's Cost of Service Report. (emphasis added)*

9 **Q. Did Staff make any alternative recommendations to MAWC's depreciation study?**

10 A. No. Staff witness Cunigan made no alternative recommendations to any of the average
11 service life or net salvage recommendations related to any non-amortized accounts.
12 Additionally, Mr. Cunigan made no recommendations on any of the depreciation rate
13 calculations for any non-amortized accounts.

14 **Q. Please explain how amortization accounting relates to general plant accounts?**

15 A. Utility depreciation accounting practices require a utility to track investment at an
16 installation year and retirement unit level within its plant accounting ledgers. However, for
17 certain asset plant accounts that are comprised of large numbers of smaller value assets,
18 the tracking of the assets at a retirement unit level is onerous for both the accounting group
19 and for the operational and administrative staff of the utility. Historically, these accounts
20 relate to a small percentage of the overall utility's investment in capital assets, but consume
21 a large amount of the plant accounting workload to accurately track the inventory of the
22 assets and to execute the retirement orders for the retirement of the small dollar assets.

23 Given the small dollar value of the individual assets, it is more prudent to track the
24 investment in certain general plant accounts at a higher level – usually being at the total

1 investment by transaction year level. With this change, the total investment by year
2 becomes the retirement unit that is subject to depreciation calculations.

3 **Q. What does MAWC propose in this regard?**

4 A. MWAC proposes to convert to the above-described amortization accounting practice for a
5 small number of general plant accounts.

6 **Q. Please outline Staff's concerns regarding the use of amortization accounting methods
7 for certain general plant accounts.**

8 A. Staff witness Cunigan claims that there is the potential to lose the ability to track the asset-
9 specific retirements when amortization accounting is used. In the view of the Staff, the lack
10 of historic retirement information compromises the ability of the depreciation consultant
11 to develop an amortization period based on the knowledge gained from the review of
12 historic retirement information.

13 **Q. Do you agree with Mr. Cunigan that your ability to develop an appropriate
14 amortization period was compromised?**

15 A. No. The accounts for which MAWC proposes to use amortization accounting are generally
16 ones that the regulated utility industry as a whole have shifted to due to the impracticality
17 of keeping detailed ledgers for all assets. For example, it is impractical to track every piece
18 of work equipment that may be on a job site, or software updates on computing software,
19 or computer monitors used by office staffs. These are assets that are frequently misplaced
20 or broken and keeping track of where each individual asset is located requires extensive
21 annual inventory counts, resulting in a large expenditure. Further, expecting the accounting
22 department of a utility to process the large number of small dollar retirements associated

1 with these items would result in a significant burden on MAWC. As a result of these
2 difficulties, the study of retirement history in these accounts historically has indicated
3 average service life estimates that were too long because of the inevitable absence of all
4 appropriate retirement transactions.

5 **Q. How have you overcome these difficulties?**

6 A. Given that most utilities have not historically been able to ensure that retirements are
7 recorded without extensive annual inventory counts, depreciation consultants recognized
8 the fact that the average service life indications of these common plant accounts were more
9 accurately determined by understanding the utilities policies and replacement procedures
10 for items such as office furniture, computer hardware and software, work equipment and
11 tools, etc. Additionally, the use of company policies and practices to determine an
12 amortization period has resulted in stability of the estimates over longer periods of time.
13 As such, many utilities have received approval for the use of amortization accounting since
14 the late 1990's for many general plant accounts, including those for which amortization
15 accounting was used by MAWC in this current application.

16 **Q. Would you agree that the average life for general plant accounts would be more
17 accurate if historic retirement information was available for analysis?**

18 A. No. In fact, my experience from over 40 years of preparing and supporting depreciation
19 studies is that reliance on the review of historic retirement orders for common plant assets
20 generally results in an inappropriately long average service life estimate.

21 **Q. Do you have any other comment on the rebuttal testimony of Mr. Cunigan?**

22 A. Yes, I note that the Staff rebuttal testimony recommended depreciation rates based on the

1 continued use of the currently approved depreciation rates. However, the Staff has not
2 identified any faults in the depreciation study presented in this case, and has not provided
3 any recommendations for any change to the Iowa curve, average service life, and net
4 salvage estimates. The currently approved life and salvage estimates were based on data
5 through 2014, which results in lives based on data that is currently six years old. This study
6 will remain in effect for a minimum of three more years, resulting in rates based on data
7 that is almost ten years old by the end of the depreciation period. Absent any evidence or
8 alternative recommendations related to non-amortized accounts, the full and
9 comprehensive depreciation study presented by MAWC provides the only evidence of
10 depreciation rates that will align the depreciation expense component of the revenue
11 requirement to the estimated consumption of the service value of the MAWC plant
12 providing utility service.

13 **IV. SURREBUTTAL TO THE REBUTTAL TESTIMONY OF MR. ROBINETT**

14 **Q. Please summarize the Rebuttal Testimony of OPC witness Robinett?**

15 **A.** Mr. Robinett makes the following three recommendations in his Rebuttal Testimony:

- 16 • Support for Staff’s recommendation for continued use of the current existing
17 depreciation rates²;
- 18 • General agreement with Staff’s position to not approve amortization accounting for
19 certain general plant accounts;³ and,
- 20 • Concerns with the Staff review of the MAWC depreciation study⁴.

² Rebuttal Testimony of John. A. Robinett, page 1, line 17.

³ Rebuttal Testimony of John. A. Robinett, page 3, line 9.

⁴ Rebuttal Testimony of John. A. Robinett, page 3, line 9.

1 **Q. Is your response to the recommendations of Mr. Robinett with regard to the**
2 **continued use of the current depreciation rates the same as your rebuttal comments**
3 **to the Rebuttal Testimony of Mr. Cunigan?**

4 A. Yes. However, I note Mr. Robinett’s allegation that the continued use of the current rates
5 is the “*only option that the Commission should consider since the Staff was unable to verify*
6 *MAWC’s results*”⁵. This is incorrect. As noted previously in this testimony, subsequent to
7 the filing of Staff’s COS Report, Staff was able to “replicate similar results to that of
8 MAWC witness Larry E. Kennedy”. Further, the data provided by MAWC in response to
9 Data Request No. 0093 would have allowed any party, including Mr. Robinett, to conduct
10 an in-depth analysis of the depreciation study, if he viewed this as valuable. All data
11 required to test the average service life, net salvage estimates and the depreciation
12 calculations were provided in response to Data Request 0093. The retirement rates
13 associated with the smoothed Iowa curves are widely available in the public domain
14 through the publication of the textbook *Depreciation Systems* and the NARUC depreciation
15 manual. As such, I do not agree with Mr. Robinett’s position that “Staff is the only party
16 besides the Company that is currently capable of performing a depreciation study on the
17 utility assets”. The fact is that most depreciation consultants either have depreciation
18 software that can make the calculations or can make the calculations and graphing within
19 Microsoft Excel and Access.

20 **Q. Is your response to the recommendations of Mr. Robinett with regard to the**
21 **recommended rejection of amortization accounting the same as your rebuttal**
22 **comments to the Rebuttal Testimony of Mr. Cunigan?**

⁵ Rebuttal Testimony of John. A. Robinett, page 2, lines 1-2.

1 A. Yes.

2 **Q. Does this conclude your surrebuttal testimony?**

3 A. Yes, it does.