

Exhibit No.: _____
Issue: Depreciation
Witness: Thomas J. Sullivan
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Sponsoring Party: Missouri Gas Energy
Date Testimony Prepared: December 11, 2006
Case No: GR-2006-0422

**Before the Public Service Commission
of the State of Missouri**

Surrebuttal Testimony

Of

Thomas J. Sullivan

On Behalf of Missouri Gas Energy

Jefferson City, Missouri

December 2006

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

2 A. Thomas J. Sullivan, 11401 Lamar, Overland Park, Kansas 66211.

3 **Q. Are you the same Thomas J. Sullivan who filed direct and**
4 **rebuttal testimony in this case on behalf of Missouri Gas Energy**
5 **(“MGE” or “Company”)?**

6 A. Yes, I am.

7 **Q. What is the purpose of your surrebuttal testimony in this matter?**

8 A. I will address the three issues in connection with the rebuttal testimony of Mr.
9 Greg Macias of the Missouri Public Service Commission Staff. These issues are:

- 10 1. Mr. Macias’ Rebuttal Schedule GEM-1 is flawed and is an
11 inaccurate representation of my analysis of regional companies.
- 12 2. In Mr. Macias’ discussion of his Rebuttal Schedule GEM-1, he
13 mischaracterizes and/or confuses my testimony, positions taken by
14 the Staff in the prior MGE rate case, and the bases upon which my
15 average service life recommendations are based. He fails to
16 mention that the regional average is not the sole basis upon which I
17 rely for a number of accounts and makes no attempt to explain why
18 the existing ASLs, which Staff recommended in Case Nos. GR-
19 2001-292 and GR-2004-0209 and form the basis for many of the
20 rates that the Company is proposing, are no longer appropriate for
21 MGE.

1 3. Mr. Macias mischaracterizes my use of the simulated plant balance
2 method by taking statements from the June 2005 Depreciation
3 Report out of context.

4 **Q. Do you sponsor any schedules with your surrebuttal testimony?**

5 A. Yes, I sponsor Surrebuttal Schedule TJS-1 – Correction of Macias’ Rebuttal
6 Schedule GEM-1. This schedule was prepared under my supervision and
7 direction.

8 **Q. Please explain how Mr. Macias’ Rebuttal Schedule GEM-1 is**
9 **flawed.**

10 A. His Rebuttal Schedule GEM-1 is flawed for the following reasons:

11 1. His first footnote in Rebuttal Schedule GEM-1 implies that the
12 numbers in the “low”, “high”, and “average” columns are taken
13 from Schedule TJS-2, Table 3-4. This is not true. The figures
14 shown in the “low”, “high”, and “average” columns in Rebuttal
15 Schedule GEM-1 are not taken from my Schedule TJS-2, but are
16 instead based on his erroneous attempt to correct my analyses in
17 that table.

18 2. Mr. Macias’ did not correct the average service lives proposed by
19 the Company in his Rebuttal Schedule GEM-1, even though my
20 staff communicated those corrections to him with sufficient time to
21 do so. This results in an apples and oranges comparison and
22 ultimately contributes to his mischaracterization of my
23 recommended ASLs.

1 3. Rebuttal Schedule GEM-1 and his rebuttal testimony falsely imply
2 that the regional ASLs were the only consideration in my
3 recommended depreciation rates.

4 **Q. Please describe the error in Mr. Macias' correction of the "low",**
5 **"high", and "average" regional ASLs.**

6 A. In my rebuttal testimony¹, I give credit to Mr. Macias for discovering a
7 calculation error in Table 3-4, Summary of Regional Gas Depreciation Rate
8 Survey, Page 13. A formula was incorrectly calculating the regional estimated
9 average service life (Column AN). However, Mr. Macias does not properly
10 correct this error. Mr. Macias excludes the depreciation rates for the general plant
11 accounts for Kinder Morgan that were appropriately included in my analyses
12 before and after the correction.

13 **Q. Please explain what ASLs should be in the column that Mr.**
14 **Macias identifies as "Company" in Rebuttal Schedule GEM-1.**

15 A. The miscalculation of average service lives only affects my recommended ASLs
16 for those accounts where I base my recommended average service life solely on
17 consideration of regional averages. This impacted three accounts: Accounts 375,
18 383, and 390. For Accounts 375 and 390 (Structures and Improvements), I
19 recommend a 45 year ASL. For Account 383 (Regulators), I recommend ASL of
20 42 years. I communicated these specific changes to Mr. Macias prior to submittal
21 of our rebuttal testimonies.

¹ Thomas J. Sullivan Rebuttal Testimony, Page 2, Lines 1-6.

1 **Q. Have you corrected Mr. Macias' Rebuttal Schedule GEM-1 for**
2 **these two errors?**

3 A. Yes, I have. These corrections are reflected in my Surrebuttal Schedule TJS-1. In
4 Surrebuttal Schedule TJS-1, I show the correct low, high, and average regional
5 ASLs that tie back to my corrected Schedule TJS-2 submitted with my rebuttal
6 testimony. In addition, in Surrebuttal Schedule TJS-1, I use the correct Company
7 proposed average service lives for Accounts 375, 383, and 390 as shown in my
8 rebuttal testimony.

9 **Q. Did you make any other revisions to your direct testimony in your**
10 **rebuttal testimony that is pertinent to issues raised in Mr. Macias'**
11 **rebuttal testimony?**

12 A. Yes, I also inadvertently left out the net salvage allowances for the general plant
13 accounts, specifically for Accounts 390, 392, and 396. In my rebuttal testimony, I
14 propose the same net salvage allowance for these accounts, 40 percent, 10
15 percent, and 20 percent, respectively, that I recommended in the prior
16 depreciation report I performed for MGE (June 2000 Report). Mr. Macias'
17 recommendations are similar. Mr. Macias recommends a net salvage allowance
18 of 0 percent, 10 percent, and 25 percent for Accounts 390, 392, and 396. Overall,
19 these differences are minimal, about \$5,800.

20 **Q. Please explain how Mr. Macias mischaracterizes the bases for the**
21 **Company's recommended ASLs in his rebuttal testimony.**

1 A. Mr. Macias' Rebuttal Schedule GEM-1 is misleading and mischaracterizes not
2 only my testimony but positions taken by the Staff in prior MGE rate cases. In
3 discussing Rebuttal Schedule GEM-1, Mr. Macias further mischaracterizes the
4 bases that underlie my average service life recommendations by failing to
5 mention that regional averages are not the sole basis upon which I relied.

6 Mr. Macias states on Page 3 of his rebuttal testimony:

7 "Staff would be remiss not to point out that all but three of the Company's
8 selected average service lives are below the regional industry average,
9 thereby generating higher depreciation expense."

10 This statement may lead one to believe that my regional survey results are
11 at odds with my recommended ASLs and that the regional survey results are the
12 primary analysis that I relied upon. This statement further implies that I set my
13 recommended ASLs below the regional averages in order to generate higher
14 depreciation expense. This is simply not true and is a gross mischaracterization of
15 my testimony and schedules.

16 **Q. How did you determine your recommended ASLs for each**
17 **account?**

18 A. In the last column of Surrebuttal Schedule TJS-1, I summarize the basis for my
19 recommended ASL for each account. This information was provided in my direct
20 testimony and schedules. As indicated in my direct testimony, I used a
21 combination of techniques for the depreciation rates for which I recommended a
22 change from the existing depreciation rates: Company-specific data (which I use
23 in my simulated plant balance analyses), results of the regional survey, and

1 experience and judgment. Moreover, on 8 of the 18 accounts, I did not
2 recommend any change to the existing average service lives. These accounts are
3 highlighted in Surrebuttal Schedule TJS-1. In Mr. Macias' rebuttal testimony, he
4 would have one believe that I somehow arbitrarily recommended depreciation
5 rates lower than the regional survey averages. This is simply not true.

6 **Q. What is the significance of the accounts where you recommend no**
7 **change in ASLs?**

8 A. This is significant because the existing average service lives for these eight
9 accounts are based on Staff's recommendations in Case Nos. GR-2001-292 and
10 GR-2004-0209. The existing ASL for Account 394 – Tools is based on Staff's
11 (Ms. Jolie Mathis) actuarial analysis of MGE-specific data in Case No. GR-2004-
12 0209. The Company's recommended ASLs for the remaining seven accounts
13 were based on Staff's study of Laclede in Case No. GR-2001-292.

14 I should also point out that Mr. Macias makes no attempt to explain why
15 the ASLs that Staff recommended in Case Nos. GR-2001-292 and GR-2004-0209
16 are no longer appropriate for MGE. The primary difference between Mr.
17 Macias' recommended depreciation rates and the existing depreciation rates is
18 simply because the Staff has yet again changed its definition of surrogate.
19 Moreover, Mr. Macias is recommending a change (from 19 years to 27 years) to
20 Account 394's existing ASL, which is based on Company-specific data and an
21 actuarial analysis sponsored by Staff witness Ms. Mathis. In a deposition taken
22 on June 9, 2004, Page 38, Lines 3 through 7, Ms. Mathis stated:

1 "Not only was there a visual fit by the software [for Account 394] but the
2 result that I got seemed to be more in line when looking at other
3 comparable companies for that account, and the 19-year life seemed
4 reasonable to me for that account."

5 Based on Mr. Macias' direct testimony on Pages 5-6, , it would appear that
6 Mr. Macias made no attempt to do any actuarial analysis on Account 394 or any
7 of the other Company's accounts.

8 **Q. Do your recommended ASLs fall within the "low" and "high"**
9 **range of the regional industry norms?**

10 A. Yes, they do – for every single account.

11 **Q. Should care be exercised when using regional or surrogate**
12 **averages?**

13 A. Yes. Depreciation rates by their very nature should only change gradually. They
14 should not be changed every time a new regional or surrogate average is
15 computed, especially if the sample group is changed (as has been done by Staff in
16 three of the last four rate cases the Company has filed). Regional or surrogate
17 averages should be treated as one consideration, not the sole consideration,
18 especially to the extent Company-specific data are available.

19 **Q. Should Company-specific data carry greater weight than regional**
20 **or surrogate averages?**

21 A. Yes. Company-specific data, when it is available, is preferable to surrogate or
22 another company's data, even if that Company data is not "perfect" or even

1 complete. Company-specific data should have priority over surrogate data. In my
2 direct and rebuttal testimony, I have clearly shown that there is Company-specific
3 data that should be considered in determining ASLs for MGE. The Staff has
4 repeatedly and rigidly argued that they will only consider Company-specific data
5 in the context of one approach, actuarial or retirement analysis, when it comes to
6 MGE. Further, Mr. Macias appears to be contradicting actuarial analysis
7 performed by the Staff witness in MGE's last rate case where Company-specific
8 data was used to make a recommendation for Account 394. As indicated in my
9 rebuttal testimony, the Staff has not applied the same standards to Atmos. The
10 Staff has set unreasonable conditions for MGEs data that I believe are at odds
11 with the direction that the Commission has given both the Company and Staff.

12 **Q. Please explain how Mr. Macias' mischaracterizes your use of the**
13 **simulated plant balance method.**

14 A. On Page 9 of Schedule TJS-2 (the June 2005 Depreciation Report), I discuss the
15 results of my simulated plant balance analyses for Account 380, Services. Mr.
16 Macias selectively quotes from this section regarding problems and observations
17 with the data. MGE does not carry sufficient detail in its records regarding the
18 types of services (plastic, bare steel, protected steel, etc.). I state on Page 9 of
19 Schedule TJS-2, "The average physical life of services may vary depending on
20 the material. The use of a simulated plant balance analysis results in an aggregate
21 service life that may not be indicative of the account, especially of the property
22 currently in service." This problem, or issue, would still exist even if MGE had
23 actuarial data.

1 Similar to MGE, it appears that Staff had no data to distinguish between
2 metallic and non-metallic services when they analyzed Ameren's services.
3 Moreover, Staff found that metallic (steel) and non-metallic (plastic) services to
4 have the same average service lives in both Aquila and Laclede's cases.
5 Therefore, Mr. Macias is making a distinction that has no material impact on the
6 results and is not even distinguished by Staff in the surrogate companies he uses.
7 Staff applies one standard to MGE that Staff has not applied to the other
8 companies regulated by this Commission.

9 **Q. Please summarize your surrebuttal testimony?**

10 A. Page 2 through Page 3, Line 16 of Mr. Macias' rebuttal testimony and his
11 Rebuttal Schedule GEM-1 are flawed and misrepresent the ASLs I recommend in
12 this matter. Surrebuttal Schedule TJS-1 is an accurate representation. Further,
13 depreciation rates should not be changed simply based on the Staff's whim with
14 regard to what surrogate companies should be used. When available, even if it is
15 not perfect or does not meet some arbitrary standard, Company-specific data
16 should be used and given consideration in the development of MGE's
17 depreciation rates, including ASLs. The ASL analyses in my direct and rebuttal
18 testimony include consideration of Company-specific data or information that
19 provides important insight into the life characteristics of MGE's facilities. Staff
20 ignores this data and, based on the unreasonable standard which they have set,
21 will apparently continue to ignore this data indefinitely. This is clearly not
22 reasonable. It is especially unreasonable in light of Staff's position on Atmos.

1

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

3 A. Yes, at this time.


In the Matter of Missouri Gas Energy's
Tariff Sheets Designed to Increase Rates
for Gas Service in the Company's Missouri
Service Area.

Case No. GR-2006-0422

[illegible]

THOMAS J. SULLIVAN

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Notary Public

NOTARY PUBLIC

STATE OF KANSAS

SHELLY HOFFMAN
My Appt. Exp. 2-6-08

