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**MISSOURI PUBLIC SERVICE COMMISSION**

**REGULATORY REVIEW DIVISION**

**UTILITY SERVICES**

**SURREBUTTAL TESTIMONY**

**OF**

**ARTHUR W. RICE, PE**

Staff Exhibit No. 26  
Date 2-21-12 Reporter SL  
File No WR-2011-0337

**MISSOURI-AMERICAN WATER COMPANY**

**CASE NO. WR-2011-0337**

Jefferson City, Missouri  
February 2, 2012

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**ARTHUR W. RICE, PE**  
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1 **St. Joseph Understated Depreciation Reserves**

2 Q. Has MAWC provided detailed plant and depreciation reserve records for the  
3 St. Joseph facility that Staff accepts as sufficient evidence to show that the write off of the  
4 unrecovered plant and cost of removal resulting from the year 2000 retirement of a water  
5 treatment facility was conducted by the Company such that Staff's computed rate base was  
6 reduced by \$3,177,861, as discussed in your Rebuttal Testimony?

7 A. Yes.

8 **Response To Company Witness Mr. John Spanos**

9 Q. Does Mr. Spanos agree with Staff that MAWC's overall Company book reserves  
10 exceed the overall Company theoretical reserves by approximately \$15 million?

11 A. Yes. Mr. Spanos' Rebuttal Testimony, pages 6 through 8, demonstrates he is  
12 aware that MAWCs depreciation reserves are over-accrued by approximately \$15 million.

13 Q. Is Staff's method of estimating the size of the over-accrual consistent with  
14 Mr. Spanos' method of estimating the over-accrual?

15 A. Yes. Staff used the same calculation Mr. Spanos used.

16 Q. What method was used by Staff and Mr. Spanos to compare MAWC's book  
17 reserve to the theoretical reserve?

18 A. The remaining life method and the life span technique.

19 Q. Why did Staff choose this method and technique to estimate the size of MAWC's  
20 over-accrual?

21 A. For determining the existence of an over-accrual, Staff needed a high-end  
22 estimate of theoretical reserve. If the booked reserves are larger than this high-end estimate,  
23 Staff can be confident that MAWC has sufficient reserves to cover a shortfall that may occur

1 from an individual facility. Use of the remaining life method with the life span technique relies  
2 on the assumption that existing plant will continue to be replaced until a given point in time, and  
3 at that time, all plant of all ages will be simultaneously retired and removed. Thus, use of the  
4 remaining life method with the life span technique produces a theoretical reserve at the high end  
5 of reasonable estimates, which is appropriate for purposes of determining the existence of an  
6 over-accrual.

7 Q. Is this approach for determining the existence and size of an over-accrual  
8 consistent with estimates made by MAWC?

9 A. Yes. This approach was used by MAWC in its December 31, 2008, depreciation  
10 study. This approach is also adopted by Company Witness Mr. Spanos in his Rebuttal  
11 Testimony in this case.

12 Q. Does Mr. Spanos testimony show that sufficient depreciation reserves exist  
13 across all plant accounts in aggregate?

14 A. Yes.

15 Q. Is MAWC's request for recovery of a Platte County (Parkville) amortization,  
16 which is effectively additional and accelerated depreciation, consistent with Mr. Spanos'  
17 acknowledgement of a \$15 million over-accrual of MAWC's depreciation reserves?

18 A. Not at all. MAWC's \$15 million over-accrual is more than adequate to cover a  
19 2018 retirement of the Parkville facility. Even if MAWC retires and green-fields the Parkville  
20 facility in 2018, all else being equal, MAWC's reserves would still be over-accrued by  
21 approximately \$10,000,000.

22 Q. What if MAWC's Parkville account reserves are not adequate to cover the  
23 retirement and cost-of-removal of the Parkville facility?

1           A.     The Commission can, and likely should, order transfer of excess reserves existing  
2 at other facilities or accounts to cover any deficient Parkville subaccount.

3           Q.     When would that reserve transfer take place?

4           A.     If necessary to cover a deficiency, this transfer would take place after the  
5 treatment facility is removed from service and disposed of, the actual retired equipment  
6 identified, and the cost of removal and salvage amounts are known.

7           Q.     Has the Commission ordered MAWC to utilize state-wide depreciation rates for  
8 its multiple districts?

9           A.     Yes. Depreciation rates for MAWC have been consistent across all districts  
10 since the Commission ordered depreciation rates, effective January 1, 2008, in Case  
11 No. WR-2007-0216.

12          Q.     Is use of existing over-accruals to mitigate potential reserve shortfalls particularly  
13 appropriate where MAWC uses state-wide depreciation rates?

14          A.     Yes.

15          Q.     Is Staff willing to work with MAWC and potential interveners to discuss methods  
16 for carrying out a reserve transfer prior to MAWC's potential Parkville retirement?

17          A.     Yes. Because the Company has requested consolidated tariffs across all of  
18 Missouri, Staff has recommended different community systems consolidated into districts, and  
19 the Office of the Public Counsel has proposed keeping existing districts, Staff does not have a  
20 recommendation at this time for a potential reserve transfer several years in the future. The  
21 Commission and parties have until 2018 to agree on a methodology to handle transfers of  
22 reserves to balance deficiencies and excesses which occur in different parts of the Company as a  
23 result of consolidated depreciation rates. The Company as a whole has sufficient reserves.

1 Q. What should the Commission order to effectuate Staff's recommendations in  
2 this case?

3 A. (1) The Commission should **not allow special additional depreciation expense**  
4 **for the Platte County (Parkville) water treatment plant** in this rate case. If a shortfall exists  
5 in the Parkville account following retirement of the Parkville unit, then the Commission should  
6 order the transfer of reserves between accounts and facility locations to balance reserve shortfalls  
7 and excesses for out of balance reserves accounts, prior to any modification of depreciation rates  
8 in any future case brought before the Commission.

9 (2) **Continue to use the current ordered Company-wide consolidated**  
10 **depreciation rates for water and sewer** plant accounts as shown in the Staff Report Cost  
11 of Service Appendices, Schedules AR-1 and AR-2.

12 (3) As recommended in the Staff's Cost of Service report and Rebuttal  
13 Testimony of Arthur Rice, that **MAWC Conduct a depreciation study** for submission to  
14 the Commission with the Company's next rate case or within three years from the effective  
15 order date of this case. This study shall include all depreciable water and sewer plant  
16 accounts. Additionally, the definition of the retirement history to be included, the source of  
17 the historical records used in this depreciation study, and applicable distinctions in treatment  
18 among different Company tariff districts, if any, shall be submitted to the Manager of the  
19 Staff's Engineering and Management Services Unit for review 60 days prior to the Company  
20 conducting the depreciation study.

21 (4) As recommended in Arthur Rice's Rebuttal Testimony, the Commission  
22 should reject MAWC's request that the Commission authorize a **12 year amortization**

1 **period** for future accounting of the cost of American Water's Business Transformation  
2 System.

3 Q. Does this end your Surrebuttal Testimony?

4 A. Yes.

