BEFORE THE

PUBLIC SERVICE COMMISSION OF UTAH

JOINT APPLICATION OF QUESTAR GAS COMPANY, THE DIVISION OF PUBLIC UTILITIES AND UTAH CLEAN ENERGY FOR THE APPROVAL OF THE CONSERVATION ENABLING TARIFF ADJUSTMENT OPTION AND ACCOUNTING ORDERS	**Docket No. 05-057-T01**

Direct Testimony of

JACOB POUS

for

Committee of Consumer Services

MARCH 31, 2006

BEFORE THE
PUBLIC SERVICE COMMISSION OF UTAH

PSC DOCKET NO. 05-057-T01

ACRONYMS

AGA/EEI ..... American Gas Association / Edison Electric Institute
CCS ..... Committee of Consumer Services
CFR ..... Code of Federal Regulations
DPU ..... Division of Public Utilities
DUCI ..... Diversified Utility Consultants, Inc.
FERC ..... Federal Energy Regulatory Commission
GF ..... Gannett Fleming
NPSC ..... Nevada Public Service Commission
PSCU ..... Public Service Commission of Utah
USOA ..... Uniform System of Accounts

2004 Study ..... *Depreciation Study on Calculated Annual Depreciation Accruals Related to Gas Plant at December 31, 2004*
Commission ..... Public Service Commission of Utah
Company ..... Questar Gas Company
Questar ..... Questar Gas Company
Sierra ..... Sierra Pacific Power Company

BEFORE THE
PUBLIC SERVICE COMMISSION OF UTAH

PUC DOCKET NO. 05-057-T01

TABLE OF CONTENTS

SECTION I: INTRODUCTION 4

SECTION II: NET SALVAGE 9

A. GENERAL 9

B. ACCOUNT SPECIFIC 12

SECTION III: LIFE ANALYSIS 18

SECTION IV: GENERAL PLANT AMORTIZATION 20

SECTION V: TIMING AND IMPLEMENTATION OF DEPRECIATION RATES 24

PUC DOCKET NO. 05-057-T01

JOINT APPLICATION OF QUESTAR GAS COMPANY, THE DIVISION OF PUBLIC UTILITIES AND UTAH CLEAN ENERGY FOR THE APPROVAL OF THE CONSERVATION ENABLING TARIFF ADJUSTMENT OPTION AND ACCOUNTING ORDERS	**§**	**BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH**

DIRECT TESTIMONY OF JACOB POUS

SECTION I: INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Jacob Pous and my business address is 12113 Roxie Drive, Suite 110, Austin, Texas 78729.

Q. WHAT IS YOUR OCCUPATION?

A. I am a principal in the firm of Diversified Utility Consultants, Inc. ("DUCI"). A copy of my qualifications appears as Appendix A.

Q. PLEASE DESCRIBE DIVERSIFIED UTILITY CONSULTANTS, INC.

A. DUCI is a consulting firm located in Austin, Texas with an international client base. The personnel of DUCI provide engineering, accounting, economic and financial services to its clients. DUCI provides utility consulting services to municipal governments with utility systems, to end-users of utility services, and to regulatory bodies such as state public service Commissions. DUCI provides complete rate case analyses, expert testimony, negotiation services and litigation support to clients in electric, gas, telephone, water, sewer, and cable utility matters.

Q. HAVE YOU PREVIOUSLY TESTIFIED IN PUBLIC UTILITY PROCEEDINGS?

A. Yes. Appendix A also includes a list of proceedings in which I have previously presented testimony. In addition, I have been involved in numerous utility rate proceedings that

resulted in settlements before testimony was filed. In total, I have participated in well over 300 utility rate proceedings in the United States and Canada

Q. WHAT IS YOUR PROFESSIONAL BACKGROUND?

A. I am a registered professional engineer. I am registered to practice as a professional engineer in the state of Texas, as well as numerous other states.

Q. ON WHOSE BEHALF ARE YOU PROVIDING THIS TESTIMONY?

A. My testimony and recommendations are presented on behalf of the Committee of Consumer Services ("CCS") for the State of Utah.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. My testimony addresses the appropriate level of depreciation expense for the Questar Gas Company ("Questar" or the "Company") in Docket No. 05-057-T01 before the Public Service Commission of Utah ("Commission" or "PSCU"). Specifically, my testimony addresses the following key areas: depreciation life and salvage parameters for mass property plant; amortization of certain general plant proposals; and the timing of depreciation studies.

Q. PLEASE PROVIDE AN OVERVIEW OF THE COMPANY'S REQUEST.

A. The Company retained Gannett Fleming ("GF") to perform a depreciation study on its distribution and general plant. The study, entitled *Depreciation Study — Calculated Annual Depreciation Accruals Related to Gas Plant at December 31, 2004* ("2004 Study"), was based on data through December 31, 2004, and presented to the Company on January 12, 2006. The 2004 Study was performed in response to Item 13 of the Stipulation and Settlement in Docket No. 02-057-02.[1]

The 2004 Study proposes an annual level of depreciation expense of $38,400,678 based on plant as of December 31, 2004.[2] The 2004 Study also proposes for the first time a change to amortization accounting of certain general plant accounts. The Company claims that its new proposed depreciation rates would result in an approximate $4.8

[1] Settlement document in Docket No. 02-057-02 dated October 21, 2002, Appendix 2. Allocation and Rate Design Stipulation and Settlement at page 65. Item 13 states: "QGC shall perform a depreciation study within one year for consideration in future regulatory procedures."

[2] 2004 Study at page III-9.

million revenue requirement reduction when compared to the depreciation expense calculated by applying existing depreciation rates.[3]

Q. HAVE YOU REVIEWED THE 2004 STUDY?

A. Yes.

Q. BASED UPON YOUR REVIEW, PLEASE BRIEFLY SUMMARIZE YOUR CONCLUSIONS AND RECOMMENDATIONS.

A. I conclude that the 2004 Study is not well documented or supported, and proposes depreciation rates and, consequently, depreciation expense that are excessive. After review of the available information provided on a timely basis, I recommend the following:

- Net salvage for Distribution Mains and Services be increased (made less negative) than what was proposed by GF. Given the quality of the GF results, I propose two alternatives for distribution plant as of the end of 2004. The first alternative would further reduce the Company's depreciation expense by $3.0 million annually, or a total reduction of approximately $7.8 million ($4.8 + $3.0). The second, and more appropriate, alternative would further reduce the Company's depreciation expense by $4.9 million annually, or a total reduction of approximately $9.7 million ($4.8 + $4.9).
- The Company proposes for the first time to switch from depreciation accounting to amortization accounting. The initial amortization periods for certain accounts or subaccounts used by Questar are too short and need to be lengthened. The lengthening of amortization periods for certain assets results in a further reduction in depreciation expense by $138,639.
- Due to the inadequate support, documentation, and justification for the Company's proposed depreciation rates, I recommend that the Commission order the Company to perform a complete, thorough and well-documented depreciation study in conjunction with its next rate case filing. This recommendation is made with full recognition that the Commission had previously ordered the Company to

[3] Mr. McKay's Direct Testimony at page 17.

perform a depreciation study and that the 2004 Study was presented to meet that directive.

The various alternatives set forth above result in a range of additional reductions to annual depreciation expense of approximately $3.2 million to $5 million, and are provided in Schedule (JP-1). The various alternatives, including the Company's proposed reduction, are summarized in the following table.

Impact of Alternative Recommendations

Option	Company Filing	CCS			Grand Total
		Distribution Plant	General Plant	Total Adjustment	
1	$4,800,000	$3,034,018	$138,639	$3,172,657	$7,972,657
2	$4,800,000	$4,812,994	$138,639	$4,951,633	$9,751,633

Q. PLEASE DISCUSS THE ABOVE CONCLUSIONS AND RECOMMENDATIONS IN GREATER DETAIL.

A. While the 2004 Study represents a step in the right direction (lowering of depreciation rates and expense), it unfortunately is an inadequate step. The underlying basis for the Company's various mortality characteristics (life and salvage parameters), which are integral components in the development of a final depreciation rate, are not adequately supported or justified. Neither the Commission nor the customers are well served when requests of such magnitude are developed and presented in a manner that fails to present the specific underlying basis for depreciation parameters, let alone meet the Company's burden of proof on this matter. This is especially true when the 2004 Study represents the first time the Company has performed a formal depreciation analysis.

Based on the information provided by the Company, it is clear that the requested level of depreciation expense is still excessive. Given the Company's failure to present complete and detailed analyses, along with it not providing certain requested information on a timely basis, I find it necessary to recommend two alternatives for setting new depreciation rates (expense) relating to distribution plant and a separate recommendation for setting new depreciation rates (expense) relating to general plant.

The two alternative adjustments I recommend to distribution plant reflect the levels of net salvage recommended by GF in a contemporaneous depreciation case before the Nevada Public Service Commission ("NPSC") for the two major plant accounts that

represent approximately three-quarters of the total distribution plant investment. My first alternative distribution plant recommendation is based on GF's testimony in the Nevada deprecation case. In that case, GF's Western Regional Manager testified in support of net salvage levels for Sierra Pacific Power Company's ("Sierra") gas division based on the identical industry data that is the basis for the "informed judgment" upon which GF's project manager, Mr. Wiedmayer, relies upon in the Utah case. By relying on the equivalent and contemporaneous net salvage values for distribution plant as sponsored by GF in Nevada, I calculate an adjustment that reduces Questar's requested depreciation expense by $3,034,018. This alternative produces a total depreciation expense for distribution plant of $28,860,607 based on plant as of December 31, 2004.

My second alternative distribution plant recommendation adjusts the Company's net salvage to the level that I recommended in the previously noted Sierra case in Nevada for the two largest distribution plant accounts. In that case, GF and Sierra were willing to provide additional detailed information in comparison to the level of information being provided in the Utah case regarding practices, policies, procedures, and informed judgment. This more precise information allowed for a better vetting of the claimed proposals for net salvage values. Using my recommended net salvage levels in Nevada, I calculated an adjustment that reduces Questar's requested depreciation expense by $4,812,994. This results in a total annual depreciation expense of $27,081,631 based on plant as of December 31, 2004.

Regarding the Company's general plant amortization proposal, I recommend that the amortization periods be increased for several accounts or subaccounts. The adoption of longer amortization periods, as described later in my testimony, results in an annual reduction of $138,639 based on year-end 2004 plant levels.

Finally, it is critical that the Commission order the Company to perform a complete, well-documented depreciation study and submit it in conjunction with its next

rate case filing. Only when the Company is willing to present verifiable support and evidence for its numerous depreciation proposals can the Commission and Interveners effectively test whether the resulting depreciation rates (expense) are just and reasonable.

Q. WAS THE COMPANY SPECIFICALLY REQUESTED TO PROVIDE THE BASIS FOR ITS DEPRECIATION PROPOSALS?

A. Yes. For example, Schedule (JP-2) sets forth the Company's response to Data Request 1.6 issued by the Division of Public Utilities ("DPU"). As can be seen on this exhibit, the Company was specifically requested to "identify each instance where Gannett Fleming has applied informed judgment which incorporated a review of management's plans, policies and outlook, a general knowledge of the gas utility industry, and comparisons of service life and salvage value from our [*GF's*] studies of other gas utilities." This data request relates to the specific statements made at page I-4 of the 2004 Study where GF states the claimed basis for the various proposed mortality characteristics. In other words, the Company presented a very cursory statement identifying a non-descriptive, generalized concept for the basis of its proposals. When subsequently requested to provide each specific basis for its proposals in order to permit testing of the validity of each claim, it responded as follows:

> "It would be too numerous to state each instance where informed judgment was applied during a study." ... Gannett Fleming conducts numerous depreciation studies for its clients each year and has assembled a file containing the depreciation parameters used by other gas companies in the U.S. for which Gannett Fleming has conducted depreciation studies." [Emphasis added]

This failure to provide the specific basis for the Company's proposals leaves limited items of quantifiable information that appears to be the basis of the Company's proposals. That one clearly identifiable item of support is a limited comparison of mortality characteristics by GF in its database of other depreciation studies that it has performed for other gas utilities.

SECTION II: NET SALVAGE

A. GENERAL

Q. WHAT IS NET SALVAGE?

A. Net salvage, as defined by FERC's Uniform System of Accounts ("USOA"), is as follows:

> Net salvage value means the salvage value of property retired less the cost of removal.[4]

"Salvage" and "cost of removal" are defined in 18 CFR Part 201 as follows:

> Salvage value means the amount received for property retired, less any expenses incurred in connection with the sale or in preparing the property for sale; or, if retained, the amount at which the material recoverable is chargeable to Materials and Supplies, or other appropriate amount.
>
> Cost of removal means the cost of demolishing, dismantling, tearing down or otherwise removing gas plant including the cost of transportation and handling incidental thereto.

One additional definition is required in order to properly follow the USOA Gas Plant Instructions. That definition is for "replacing" or "replacement," and is as follows:

> "Replacing" or "replacement," when not otherwise indicated in the context, means the construction or installation of gas plant in place of property retired, <u>together with the removal of the property retired</u>." (Emphasis added)

In other words, "net salvage" is simply the value received for the sale, reuse, or reimbursement of retired property (gross salvage) less the cost of retiring such property (cost of removal), whether the retirement reflects demolition of the item of plant or only the accounting transaction for retiring an item of property in place (abandonment). However, limited levels or no cost of removal should occur when the removal of the property retired occurs with replacement activity. This situation conforms to USOA Gas Plant Instruction 10B(2). That instruction recognizes cost of removal as being "appropriate" when not accompanied by replacement activity. However, the crediting of the plant account for the retirement shall occur with or without a replacement.

[4] 18 Code of Federal Regulations ("CFR") Part 201, Definitions.

Q. CAN YOU ILLUSTRATE USING AN ACTUAL EXAMPLE OF HOW QUESTAR'S PROPOSED NET SALVAGE IMPACTS REVENUE REQUIREMENT?

A. Yes. For Account 380-Distribution Services, the Company has requested a negative 90% net salvage. Given the plant balance of $259 million, the Company's proposed net salvage figure would result in approximately $233 million ($259 million x 90%) of revenue requirement over the life of the investment above the recovery of the original $259 million investment.[5] The proposed annual depreciation rate for this account is 3.86% to recover all proposed amounts (both investment and net salvage).[6] Absent the impact of any negative net salvage (a zero level of net salvage), the annual depreciation rate declines to only 1.32%.[7] The difference in rates applied to the $259 million plant balance would result in approximately a $6.6 million annual revenue requirement impact for this account alone.

Q. WHAT PERIOD HAS THE COMPANY CHOSEN TO ANALYZE ASSOCIATED WITH ITS NET SALVAGE ANALYSIS?

A. The Company has analyzed a 14-year period, 1990 through 2003.[8]

Q. HAVE YOU REVIEWED ALL THE INFORMATION PRESENTED BY THE COMPANY IN SUPPORT OF ITS NET SALVAGE REQUEST?

A. Yes. The information provided is inadequate to support or demonstrate the appropriateness of its request for an overall negative 40% net salvage for distribution and general property.[9] Questar's depreciation study included $477 million for negative net salvage related to gas mass property over the life of the investment.[10]

Q. PLEASE SUMMARIZE YOUR RECOMMENDATION CONCERNING QUESTAR'S PROPOSED NET SALVAGE VALUES FOR MASS PROPERTY.

A. Questar's proposed net salvage is flawed and insufficiently substantiated. The proposals set forth in the 2004 Study produce excessive levels of negative net salvage. I

---

[5] 2004 Study at page III-3.
[6] *Id.* and at page III-6.
[7] *Id*., with a zero level of net salvage.
[8] Response to CCS 2.9.
[9] 2004 Study at page III-3.
[10] *Id*., mass property includes distribution and general plant.

recommend two alterative reductions to Questar's proposed depreciation expense based on recommended adjustments to its proposed net salvage levels. The stand-alone impact of my net salvage recommendations is a reduction of either $3.0 million or $4.8 million in annual depreciation expense.

Q. WHAT ACCOUNTS ARE YOU RECOMMENDING CHANGES TO FOR NET SALVAGE?

A. I am recommending changes to two mass property accounts. Those adjusted accounts are listed below.

Comparison of Net Salvage %

		CCS	
Account	**Questar Proposal**	**Alternative 1**	**Alternative 2**
376 Gas Distribution Mains	-45	-30	-20
380 Gas Distribution Services	-90	-70	-60

Q. IN THE AREA OF NET SALVAGE, IS THE IMPACT OF THE COMPANY'S PROPOSAL CONCENTRATED IN A FEW ACCOUNTS?

A. Yes. Out of the approximately $477 million of negative net salvage requested by the Company, approximately $466 million (about 98%) is concentrated in accounts 376-Distribution Mains and 380-Distribution Services.

Q. BASED ON THE INFORMATION PROVIDED, IS THE COMPANY'S REQUEST FOR NEGATIVE NET SALVAGE FOR THESE TWO MAJOR ACCOUNTS REASONABLE AND APPROPRIATE?

A. No.

B. <u>ACCOUNT SPECIFIC</u>

Q. WHAT SPECIFICALLY HAS THE COMPANY REQUESTED FOR ACCOUNT 376-DISTRIBUTION MAINS?

A. Distribution Mains represent the largest single plant account. The Company requests a negative 45% net salvage, or $233,265,831 of net salvage to be recovered from customers over the life of the investment. The impact of this request is that approximately 12%, or

$4.7 million of annual depreciation expense is due to the requested negative 45% net salvage.

Q. WHAT SPECIFIC BASIS DID THE COMPANY PROVIDE IN SUPPORT OF A NEGATIVE 45% NET SALVAGE?

A. There are potentially three identifiable components of information available that the Company has provided in support of its proposal. The items of information provided are the historical data as reported by the Company, a limited survey of the values proposed by GF in other jurisdictions and the "rough notes" that Mr. Wiedmayer took during his site visit to the Company.

Q. DO THE HISTORICAL DATA FOR THIS ACCOUNT JUSTIFY A NEGATIVE 45% NET SALVAGE?

A. No. The historical database relied upon by the Company covers the period 1990 through 2003.[11] While the historical data indicates a wide range of values, the average is a negative 37%.[12] Moreover, the *trend* in the historical values is to a less negative level. The trend in the data is important. Indeed, GF has stated its position in other jurisdictions that it is important to ascertain if there is a trend in the data when making estimations of the appropriate level of net salvage for plant investment.[13] Thus, a value ranging from approximately 30% to 35% would be more indicative of the historical data, taking into account the selection process sponsored by GF in other jurisdictions.

Q. DOES GF'S LIMITED DATABASE OF OTHER UTILITIES SUPPORT THE COMPANY'S PROPOSED NEGATIVE NET SALVAGE?

A. No. While the range relied upon by GF is from a negative 10% to a negative 100%, the dispersion and average indicates that a negative 30% to a negative 35% value would be more indicative of even GF's limited industry data.[14] In fact, the median and mode values associated with GF's limited industry data indicate that a value less than negative 30%

[11] 2004 Study at page I-4.

[12] Response to CCS 2.9.

[13] For example, Mr. Spanos' (Mr. Wiedmayer's superior) rebuttal testimony in Docket Nos. 03-10001/03-10002 at page 34 before the NPSC.

[14] Response to DPU 1.6.

would be appropriate. This is further reinforced by a review of a broader industry survey.[15]

Q. DID THE COMPANY PROVIDE ANY INFORMATION IN ITS "ROUGH NOTES" THAT WOULD SUPPORT THE NEGATIVE 45% NET SALVAGE?

A. No.[16]

Q. PLEASE SUMMARIZE YOUR FINDINGS REGARDING THE NEGATIVE 45% NET SALVAGE FOR ACCOUNT 376.

A. Account 376 represents not only the largest plant investment account, but also the account that the Company seeks the greatest level of net salvage to be recovered from customers. The Company's testimony, exhibits, workpapers and data responses do not provide any valid support for a negative 45% value. The value is excessive when tested against the actual historical data, the trends in the data, GF's limited database for other utilities, a more robust database of depreciation statistics for the industry or based on any identified policy, plan, procedure, etc. of the Company. Simply put, the Company has presented no information which would warrant a negative net salvage as negative as 45%. The unidentifiable basis for the Company's selection should be rejected by the Commission.

Q. WHAT DO YOU RECOMMEND?

A. I am recommending two alternatives. The first alternative for this account would be a negative 30% net salvage, which corresponds to the level of net salvage that GF sponsored in a contemporaneous case before the NPSC for Sierra. Again, it is worth noting that GF's witness in that proceeding relied on the identical GF limited database as Mr. Weidmayer did for this case. Moreover, at least GF in the NPSC proceeding was willing to provide some evidence relating to its selection process. Even that limited information is far more informative than the striking lack of information provided by the Company in this proceeding. Reliance on a negative 30% net salvage as recommended by GF in Nevada results in a reduction of $1,571,797 to annual depreciation expense based

[15] American Gas Association/Edison Electric Institute ("AGA/EEI") A Survey of Depreciation Statistics, 1998-1999. This survey indicates less negative net salvage values than that proposed by the Company, whether the entire database is relied upon, or only the more current values within the survey are relied upon.

[16] Response to DPU1.7.

on plant as of December 31, 2004. It would also result in an annual depreciation rate of 1.97% for Distribution Mains.

The second alternative, and in my opinion the more appropriate alternative, would be to set the net salvage level for this account at a negative 20%. This recommendation recognizes the Company's accounting policies associated with booking costs to the cost of new installations when replacement activities occurs, while incurring some level of cost removal in the instances where the Company abandons pipe in the ground.[17] Reliance on a negative 20% net salvage value for this account results in a reduction of $2,619,662 based on plant as of the end of 2004 and a corresponding 1.77% annual depreciation rate.

Q. WHAT SPECIFICALLY HAS THE COMPANY PROPOSED FOR ACCOUNT 380-DISTRIBUTION SERVICES?

A. This account is the Company's second largest plant account and reflects the Company's second largest request for negative net salvage. The Company's request for approximately $233 million of negative net salvage for this account over the life of the facilities is based on its proposal to utilize a negative 90% net salvage. In other words, the Company is seeking $1.90 for every dollar investment it places into service.

Q. WHAT IS THE COMPANY'S BASIS FOR ITS SIGNIFICANT LEVEL OF REQUESTED NEGATIVE NET SALVAGE?

A. Again, the limited information provided by the Company in its testimony, exhibits, workpapers and data responses provides no meaningful support and justification for this high level of negative net salvage.

Q. PLEASE DISCUSS THE HISTORICAL DATA ASSOCIATED WITH THIS ACCOUNT.

A. The historical database reviewed by GF for its analysis is poor in quality. In fact, for the period 1997 through 2001, the Company does not report <u>any</u> retirement activity (even though it does report a few years' of cost of removal and gross salvage during the same

[17] Response to DPU 1.25 and CCS 2.31. While the Company claims there are several costs associated with abandonment of property, many of these costs most likely are more appropriately charged to the cost of any new replacement activity rather than as cost of removal.

corresponding period).[18] The available historical data do result in an annual net salvage ranging from a negative 53% to a negative 310%. This extremely wide range is indicative of a questionable database. In fact, as a depreciation professional, I find it hard to believe that GF would have actually relied on the historical database for any meaningful portion of its proposal given the poor pattern, frequency and materiality associated with the historical data.

Q. DID GF'S LIMITED INDUSTRY DEPRECIATION STATISTIC DATABASE PROVIDE REASONABLE SUPPORT FOR THE COMPANY'S PROPOSAL?

A. No. Again, the range set forth in GF's limited database is quite extensive. In fact, it ranges from a negative 25% to a negative 200%. Indeed, just about any value could fit within this size range. However, a review of the dispersion of values within the range and the consideration of potential mean, median and mode of the values would result in industry values of a negative 30% to negative 60% as being more indicative of the industry.[19]

Q. DO THE COMPANY'S NOTES ASSOCIATED WITH MR. WIEDMAYER'S SITE VISIT PROVIDE ANY INSIGHT INTO THE SUPPORT OR JUSTIFICATION FOR THE SELECTION OF A NEGATIVE 90% NET SALVAGE?

A. No.[20] As was the situation for Distribution Mains discussed previously, the Company's accounting policies associated with replacement activity and abandonment would dictate that a negative 90% net salvage value is inappropriate.

Q. WHAT DO YOU RECOMMEND?

A. I am proposing two alternatives. The first alternative is a negative 70% as proposed by GF in the contemporaneous Sierra case before the NPSC. Relying on a negative 70% net salvage value results in a reduction to the Company's proposed depreciation expense of $1,462,221 based on year-end 2004 plant levels. This alternative would also result in an annual depreciation rate of 3.30%.

---

[18] Response to CCS 2.9.

[19] Response to DPU1.6.

[20] Response to DPU1.7.

My second alternative corresponds to the value I recommended based on a review of more information provided by GF on behalf of Sierra in its current case before the NPSC. There, based on additional information that Sierra provided, I recommended a negative 60% net salvage as a conservative estimate of an appropriate net salvage value for investment in this account. Relying on a negative 60% net salvage results in a $2,193,332 adjustment to the Company's annual depreciation expense based on year-end 2004 plant levels, and a corresponding 3.01% annual depreciation rate.

Q. PLEASE SUMMARIZE YOUR TESTIMONY AS IT RELATES TO NEGATIVE NET SALVAGE FOR THE COMPANY'S TWO LARGEST PLANT ACCOUNTS.

A. The Company's investment in accounts 376-Distribution Mains and 380-Distribution Services, comprise approximately 75% of its distribution plant investment. Moreover, the Company's request for a negative 45% and negative 90% net salvage for accounts 376 and 380, respectively, produces 98% of its entire net salvage request for distribution plant. Thus, testing the overall reasonableness of the Company's proposed depreciation rates and expense for these two major accounts reflects my critical review of the meaningful portion of the expense at issue.

The Company's testimony, exhibits, workpapers and data responses clearly demonstrate that the Company has *failed* to meet any reasonable burden of proof in establishing the appropriateness of its depreciation proposals. Thus, the Commission should order the Company to develop and present a complete, and well-documented depreciation study in connection with its next general rate case filing.

My review of the information available at this time demonstrates that the Company's request for significant levels of negative net salvage is quite excessive. The Company's overall proposal to decrease depreciation expense is a step in the right direction, but falls short of reasonable levels based on the available information. Based on the two alternatives previously noted, the Company's depreciation expense request, based on year-end 2004 plant levels, should be further reduced by:

(1) $3,034,018 based on a negative 30% and negative 70% net salvage for accounts 376 and 380, respectively. These levels of negative net salvage are the same as those recommended by GF in the contemporaneous Sierra depreciation case before the NPSC.

(2) $4,812,994 based on a negative 20% and a negative 60% net salvage for accounts 376 and 380, respectively. These levels of negative net salvage are the same as recommended by me in the contemporaneous Sierra depreciation case before the NPSC.

SECTION III: LIFE ANALYSIS

Q. ARE THERE OTHER DEFICIENCIES WITH THE COMPANY'S FILING?

A. Yes. The two main categories of the depreciation study are the life analysis and the salvage analysis. As previously discussed, the Company's support for its salvage analyses is woefully inadequate. However, the Company's support and presentation of its life recommendations was basically non-existent up until I received an e-mail on March 27, 2006. The Company's depreciation study includes illustrations of life estimations and discussions of the processes in performing historical life analyses. Unfortunately, not a single life analysis calculation for determining the average service life and corresponding survivor curve for a single actual account of the Company is presented anywhere in the Company's filing.

Q. IS THIS FAILURE TO PRESENT THE LIFE ANALYSIS TYPICAL?

A. No. For example, in the contemporaneous Sierra case before the NPSC, GF presented 30 pages of specific life analyses for the Sierra's gas distribution system. Yet not one page is contained in the 2004 Study presented in this case. In fact, all that is presented is the end result of whatever analyses GF may or may not have performed. I can think of no other area of utility regulation where a utility would file a requested rate change without providing the necessary underlying data, analyses and calculations. This is especially concerning given that Questar is seeking to recover over $38 million of annual depreciation expenses from its customers. This type of presentation underscores the recommendation I have previously set forth that the Commission order Questar to perform a complete and detailed depreciation study along with extensive documentation clearly setting forth the step-by-step process it employed, and the underlying data and analyses it relied on, to arrive at each and every life and salvage value that comprise the depreciation study. The Company's presentation in this proceeding does not rise to the

level of an adequate or complete depreciation study to support a request of this magnitude.

SECTION IV: GENERAL PLANT AMORTIZATION

Q. DOES THE COMPANY ALSO SEEK FOR THE FIRST TIME THE IMPLEMENTATION OF AMORTIZATION ACCOUNTING FOR CERTAIN GENERAL PLANT ACCOUNTS?

A. Yes. As set forth on pages II-27 and 28 of the 2004 Study, the Company identifies 14 accounts or subaccounts where it is seeking to implement amortization accounting.

Q, WHAT IS THE COMPANY'S BASIS FOR ITS PROPOSED CHANGE IN THE RECOVERY OF ITS INVESTMENT FOR THESE ACCOUNTS?

A. The Company states that it is proposing to change to amortization accounting "because of the disproportionate plant accounting effort required when compared to minimal original cost of the large number of items in these accounts."[21] In other words, the Company wants to change from depreciation to amortization accounting because it perceives that it is incurring a cost in performing plant accounting efforts to keep track of the investment in these accounts without real success. It further notes that the Federal Energy Regulatory Commission ("FERC") in 1997 issued Accounting Release 15. That Accounting Release granted utilities approval for the portion of their business subject to the FERC regulation to use vintage year or amortization accounting for general plant accounts. The Company then continues and identifies the end result of its selection process for amortization periods for these selected accounts or subaccounts. The Company concludes its efforts in this area by stating that the amortization periods selected were "based on judgment".[22]

Q. DID THE COMPANY IDENTIFY WHAT JUDGMENT IT RELIED UPON?

A. No, not really. The Company simply stated that it considered as part of its judgment "the period during which the assets will render most of their service, the amortization period and service lives used by other utilities and service life estimates previously used under depreciation accounting."[23]

---

[21] 2004 Study at page I-3.

[22] 2004 Study at page II-27.

[23] Id.

Q. DO ANY OF THESE VAGUE GENERALIZATIONS HAVE ANY VERIFIABLE MEANING THAT COULD SUPPORT THE SPECIFIC VALUES PROPOSED BY THE COMPANY REGARDING AMORTIZATION PERIODS?

A. No. In fact the first generalized statement referencing the period during which the assets would render most of their service is inconsistent with the depreciation related capital recovery theory. The recovery of investment should be over the expected useful life of the investment. In other words, the Company has made an admission that it is employing artificially short amortization periods.

Q. IS THE COMPANY IN FACT UTILIZING ARTIFICIALLY SHORT AMORTIZATION PERIODS?

A. Yes. A review of the 2004 Study clearly demonstrates that in many instances the amortization period selected by the Company understates the actual expected service life for its investment.[24] A good example of the inadequate amortization period, based on actual data, can be seen on Schedule (JP-3). This schedule sets forth page A-41 from the Company's 2004 Study and represents account 397.3-Communication Equipment-Base Station. This is an account representing approximately $16 million of investment. The Company proposed a 10-year amortization period for this account. However, as can be seen on this schedule, the Company has investment for the period 1974-1994 still on its books, which is beyond its proposed 10-year amortization period. In fact, approximately 44% of the investment in this account is beyond the 10-year amortization period. Therefore, when the Company claims that it based its recommendation in part on the "period during which the assets will render most of their service" it has ignored this particular parameter in selecting the amortization period for this subaccount.

Q. DOES THE COMPANY ALSO CLAIM THAT WHEN GENERAL PLANT ASSETS ARE RETIRED, THEY ARE NOT ALWAYS REMOVED FROM ITS BOOKS?

A. Yes.[25] Unfortunately, the Company provides no empirical analysis or data that would substantiate the amount of retired assets that are still on the Company's books. This claim represents an unsubstantiated generalized statement that does not rise to the level of

[24] 2004 Study at A-28 through A-44.

[25] Response to CCS 2.37

evidence. It does not adequately support the very short amortization period proposed by the Company.

Q. HAS THE COMPANY APPROPRIATELY RELIED ON FERC ACCOUNTS RELEASE 15 FOR ITS PROPOSED AMORTIZATION PERIODS?

A. No. Attached as Schedule (JP-4) is FERC Accounting Release 15. As can be seen, the Company proposal does not comply with FERC Accounting Release 15. For example, item number 3 indicates that the depreciation expense should be over the investment's useful life. This is directly contrary to the Company's claim that it chose a period that reflects "most" of the asset's useful life. Also reflected in item 3 is a requirement that there be "no change in depreciation rates resulting from the adoption of the vintage year [amortization] accounting." The Company has in no way demonstrated that its proposed amortization periods do not result in changes in effective depreciation rates, thus violating the FERC Accounting Release 15.

Q. ARE YOU OPPOSED TO AMORTIZATION ACCOUNTING?

A. No. However, the concept of amortization accounting should not be taken as carte blanche for a utility to artificially shorten the effective useful life of the investments for purposes of calculating depreciation recovery periods. It is incumbent upon the Company to demonstrate not only its compliance with FERC Accounting Release 15, but also that its proposals will result in just and reasonable rates. The Company has again failed in this area.

Q. CAN THE COMPANY CLAIM THAT ITS AMORTIZATION PERIODS ARE REPRESENTATIVE OF AVERAGE SERVICE LIFE AND THAT PLANT CAN AND WILL CONTINUE TO BE USED BEYOND THE AVERAGE SERVICE LIFE?

A. While the Company may claim this, it does not overcome the problem associated with the extensive amount of plant beyond its proposed amortization periods that the Company still has on its books. For example, Schedule (JP-5) represents page A-40 of the 2004 Study and corresponds to account 397.1-Communications Equipment – Mobile Radio. This schedule shows that the Company has plant on its books dating 13 years beyond the amortization period it has proposed. There is no standard dispersion pattern around the average service life normally utilized by the industry that would reflect almost 10% of

plant in service at an age almost 3 times the average service life assumed for depreciation purposes. This situation further exposes the admitted artificially short amortization periods being proposed.

Q. WHAT DO YOU RECOMMEND?

A. Based on the actual information available associated with the Company's request for amortization accounting, and for purposes of this case only, I recommend the following amortization periods so as to better reflect the period during which the investment would appear to be providing service.

Account		Amortization Period		
No.	**Description**	**Company**	**CCS**	**Difference**
391.01	Office Furniture	20	20	0
391.02	Office Equipment	7	20	13
391.03	Computer Hardware	4	6	2
391.04	Computer Software	10	10	0
393	Stores Equipment	20	35	15
394.1	Small Tools	10	15	5
394.2	Shop Equipment	20	20	0
394.4	CNG Equipment	10	15	5
395	Lab Equipment	15	20	5
397.1	Mobile Radio	5	10	5
397.3	Base Stations	10	15	5
397.4	Telemetry	10	10	0
397.5	Communication Equipment – Other	10	10	0
398	Miscellaneous Equipment	15	15	0

Q. WHAT IS THE IMPACT OF YOUR RECOMMENDATIONS?

A. My recommendation for amortization periods for several of the accounts or subaccounts at issue results in a $138,639 reduction to the Company's request based on plant as of the end of 2004. It should be noted that each of the longer amortization periods that I've recommended fall within the range of values set forth in GF's limited database for the account or subaccount at issue, yet better represent the actual historical data of the Company as reflected in the 2004 Study.

SECTION V: TIMING AND IMPLEMENTATION OF DEPRECIATION RATES

Q. SHOULD DEPRECIATION STUDIES BE PERFORMED PERIODICALLY?

A. Yes.

Q. WHAT TIME INTERVAL BETWEEN STUDIES IS APPROPRIATE?

A. Unfortunately, one time period does not fit all situations. The general practice in the industry has been to perform depreciation studies every three to five years. This period of time recognizes that depreciation mortality characteristics normally do not change dramatically from year to year but can change as years of plant addition and retirement activity occur and are accumulated. The three to five year period in between depreciation studies is a reasonable guideline absent meaningful or significant levels of retirement activity or plant additions.

Q. WHAT DO YOU MEAN BY MEANINGFUL OR SIGNIFICANT LEVELS OF PLANT ACTIVITY?

A. If plant additions in between studies exceed 20% of the previous base, or if a utility retires an accumulated 5% of its plant in service, then it would be incumbent upon the utility or regulators to initiate a depreciation study. Realistically, the burden of when to file falls more heavily on the utility since it has available all the facts and figures associated with its plant investment and operations.

Q. ONCE A DEPRECIATION STUDY HAS BEEN PERFORMED, SHOULD ITS RESULTS BE IMPLEMENTED?

A. Yes. The depreciation rates associated with a depreciation study should be carefully reviewed by the Commission. Once the rates are formally approved by the Commission, they should be implemented on the books of the utility.

Q. SHOULD THE IMPLEMENTATION OF SUCH DEPRECIATION RESULTS OCCUR ONLY IN CONJUNCTION WITH BASE RATE CASES?

A. While it is desirable to have a base rate case occur at the same time as a change in depreciation rates (expense), it is not necessary. For example, the results from

PacifiCorp's most recent depreciation study (2003) were implemented in a subsequent PacifiCorp general rate case.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes. However to the extent I have not addressed an issue, method, procedure, etc. should not be construed that I am in agreement with the Company's issue, method, procedure, etc.