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October 22, 2024

VIA ELECTRONIC FILING

Hon. David Jones, Chairman
c/o Ectory Lawless, Docket Room Manager
Tennessee Public Utility Commission
502 Deaderick Street, 4th Floor
Nashville, TN 37243
TPUC.DocketRoom@tn.gov

Electronically Filed in TPUC Docket Room
on October 22, 2024 at 2:22 p.m.

RE: ***Petition of Tennessee-American Water Company to Modify Tariff, Change and Increase Charges, Fees, and Rates, and for Approval of a General Rate Increase,*** **TPUC Docket No. 24-00032**

Dear Chairman Jones:

Attached for filing please find *Tennessee-American Water Company's Rebuttal Testimonies for (1) Heath Brooks; (2) Ann Bulkley; (3) Dominic J. DeGrazia; (4) Grant Evitts; (5) Nicholas Furia; (6) Larry Kennedy; (7) Bob Lane; (8) Robert V. Mustich; (9) Robert Prendergast; (10) Charles Rea; (11) Linda Schlessman; (12) Grady Stout; (13) Harold Walker, III; and (14) John Watkins* in the above-captioned matter.

As required, the original plus four (4) hard copies will follow. Should you have any questions concerning this filing, or require additional information, please do not hesitate to contact me.

Very truly yours,

BUTLER SNOW LLP

Melvin J. Malone

clw
Attachments
cc: Bob Lane, TAWC
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TENNESSEE-AMERICAN WATER COMPANY, INC.

DOCKET NO. 24-00032

REBUTTAL TESTIMONY

OF

LARRY KENNEDY

ON

DEPRECIATION

SPONSORING PETITIONER'S EXHIBITS:

Rebuttal Exhibit LEK-1 - Summary of Accumulated Depreciation (A/D) Position by Account

REBUTTAL TESTIMONY
LARRY KENNEDY
TENNESSEE AMERICAN WATER COMPANY
DOCKET NO. 24-00032

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I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS

A. My name is Larry E Kennedy. My business address is 200 Rivercrest Drive SE, Suite 277, Calgary, Alberta, T2C 2X5.

Q. DID YOU PREVIOUSLY SUBMIT DIRECT TESTIMONY IN THIS PROCEEDING ON BEHALF OF TENNESSEE AMERICAN WATER COMPANY, INC. ("TAWC" OR THE "COMPANY") IN THIS PROCEEDING?

A. Yes. I filed direct testimony on May 1, 2024.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my rebuttal testimony is to respond to the Direct Testimony of Mark E. Garrett (the "Garrett Testimony") submitted on behalf of the City of Chattanooga. Specifically, I am addressing Mr. Garrett's recommendation that "the current depreciation and cost of removal rates continue to be authorized for recovery in customer rates."[1]

Q. ARE YOU SPONSORING ANY EXHIBITS WITH YOUR TESTIMONY?

A. Yes, I am sponsoring Rebuttal Exhibit LEK-1 - Summary of Accumulated Depreciation (A/D) Position by Account which has been filed with my testimony.

II. RESPONSE TO CITY OF CHATTANOOGA WITNESS GARRETT

Q. PLEASE DESCRIBE MR. GARRETT'S ARGUMENT IN SUPPORT OF HIS RECOMMENDATION TO LEAVE TAWC'S DEPRECIATION RATES UNCHANGED.

[1] Garrett Direct Testimony, page 35: 14-15.

A. Mr. Garrett begins with the premise that the communities Tennessee American serves have "experienced dramatic inflation" and "efforts should be made to restrain further inflation until customer incomes have had a chance to increase."[2] Mr. Garrett asserts "recovery of investment costs is a long-term process for public utilities, and there will be time to address any deficiencies in future rate cases when customer earnings are not so heavily stressed."[3]

Q. WHAT IS YOUR RESPONSE TO MR. GARRETT'S RECOMMENDATION CONCERNING THE DEPRECIATION RATES APPLICABLE TO TENNESSEE AMERICAN?

A. Witness Garrett's recommendation violates two critical regulated depreciation philosophies. First, Mr. Garrett's recommendation is not based on any reviews of the depreciation parameters, namely average service life estimates, cost of removal estimates or the depreciation methods and procedures used to develop the depreciation rate. Second, Mr. Garrett's recommendation is completely based on the use of depreciation as a utility rate mitigation mechanism, without any recognition of continued appropriateness of the depreciation rates.

Q. WHY IS A DEPRECATION RATE DIFFERENT FROM DEPRECIATION PARAMETERS?

A. The depreciation rate is the calculation of a rate based on the expected retirement properties resulting from the selection of an appropriate Retirement Dispersion Curve (Iowa Curve), the expected future costs of retirement or removal as adjusted for the expectation of any gross salvage proceeds, and the selection grouping method (for example Average Life

[2] Garrett Direct Testimony, page 35: 4-6.
[3] Garrett Direct Testimony, page 35: 8-10.

Group or Equal Life Group). As such the depreciation rate itself is not indicative of the expected life of the asset. This is confirmed in the FERC System of Accounts, as well as the NARUC manuals for water utilities in its definition of depreciation as follows:

> "Depreciation", as applied to depreciable utility plant, means the loss in service value not restored by current maintenance, incurred in connection with the consumption or prospective retirement of utility plant in the course of providing service from causes which are known to be in current operation and against which the utility is not protected by insurance. Among the causes to be given consideration are wear and tear, decay, action of the elements, inadequacy, obsolescence, changes in the art, changes in demand, and requirements of public authorities.[4]

It should be noted that the above definition of depreciation is the application of a rate which aligns to the estimates to the estimated consumption of the service value of the assets being depreciated. The above definition makes no reference to the impact of the depreciation expense on the revenue requirement.

Q. WHY IS IT IMPORTANT FOR THE DEPRECIATION PARAMETERS TO BE REEXAMINED PERIODICALLY TO DETERMINE IF THE UNDERLYING PARAMETERS REMAIN REASONABLE?

A. As noted above, the estimation of the future consumption of service value of assets is dependent upon many factors, which include physical factors, but additionally changes in technology, legislative and regulatory changes, and changes in the customer demand. Given the long-life nature of most water asset accounts, the assets within the various accounts can be greatly impacted by a number of these forces of retirement. Over time,

[4] It is noted that both the FERC Uniform System of Accounts and NARUC Uniform System of Accounts use nearly identical definitions for depreciation. The FERC definition, as quoted above, is found at Part 101, Point 12 of both the Electric and Natural Gas Uniform System of Accounts.

assets will not always retire in accordance with the estimated Iowa curve, or the actual costs of removal and receipts of gross salvage proceeds. When these variances occur, the accumulated depreciation accounts are adjusted to recognize any difference in retirements from the estimated Iowa curve or the net salvage costs or proceeds that are actually incurred. This is specifically noted in the NARUC manual which states:

> Straight-line remaining life method", as applied to depreciation accounting, means the plan under which the service value of property is charged to operating expenses (and to clearing accounts if used), and credited to the accumulated depreciation account through equal annual charges during its service life. "Remaining life" implies that estimates of future life and salvage will be reexamined periodically and that depreciation rates will be corrected to reflect any changes in these estimates.[5]

I note that the currently approved depreciation rates, which are the depreciation rates proposed in Mr. Garrett's Testimony, are based on a depreciation study that used 2007 accounting data. As such, the depreciation rates are based on 17-year-old data and operating conditions. Additionally, these accounts have not been trued-up in accordance with the above NARUC guideline since the 2007 depreciation study.

To test the need for the correction to the depreciation rates, I have reviewed the estimated life and net salvage estimates and calculated a theoretical (or calculated) requirement as of December 31, 2023, and tested this requirement against the actual accumulated depreciation balances to determine if an adjustment to the depreciation rates is necessary. These amounts by account are determined in the Detailed Depreciation Calculations as presented in Section 8 of my Depreciation Study field in Exhibit LEK-1 of this proceeding. As noted in Rebuttal Exhibit LEK-1 - Summary of Accumulated Depreciation (A/D)

[5] 1996 version of the NARUC USoA for Water Utilities at page 13.

Position by Account, the accumulated depreciation variance is significant in virtually every account. In total the accumulated depreciation accounts are in deficient position by over $22.9 million. I also note that some accounts are as much as 5,768% underfunded. This amount has been partially offset by some accounts which are significantly overfunded by as much as 175.8%. Clearly, Witness Garrett has ignored this significant intergenerational issue and his suggestion that "there will be time to address any deficiencies in future rate cases" improperly trivializes these significant historical deficiencies.

Q. PLEASE OUTLINE THE REASONS THAT THESE SIGNIFICANT ACCUMULATED DEPRECIATION VARIANCES CAUSE INTERGENERATIONAL EQUITY ISSUES.

A. As noted above and acknowledged by Mr. Garrett,[6] future customers will be responsible for the current accumulated depreciation variance of over $22.9 million over the remaining life of the assets. Moreover, adoption of Mr. Garrett's recommendations will exponentially increase this deficiency which will result in an even more dramatic impact on future depreciation rates. Each year of use of the current depreciation rates will add a substantial amount to the future deficiency that future customers will be required to bear.

Q. SHOULD THE REQUESTED DEPRECIATION RATES CONSIDER THE IMPACT ON UTILITY RATES?

A. No. Depreciation analysts understand that the selection of the depreciation parameters and methods can have an impact upon the company's requested revenue requirement. However, the overriding goal is that the depreciation estimates are correctly estimating the average

[6] Garrett Direct Testimony, page 35: 4-10.

service, the remaining life, and the net salvage requirements of the utility assets. In other words, "getting the estimates right" will ensure that the depreciation expense component of the revenue requirement will appropriately recover the capital investment over the useful life of the assets providing utility service.

Inappropriate deferrals of the recovery of utility investment will result in "getting the estimates wrong" which will cause a much greater impact on future customers to finance an inappropriate and unfair amount of the depreciation expense related to depreciation rate true-ups caused by the inappropriate estimates in prior studies. While no study will ever forecast the depreciation parameters perfectly as it is only after the assets are retired that the actual life and costs of removal of the asset are actually known, the intentional deferral of appropriately estimated depreciation expense will be a sure way of causing intergenerational inequities to future customers.

Q. HOW CAN DEPRECIATION PARAMETERS BE SELECTED IN ORDER TO PROVIDE INTERGENERATIONAL EQUITY?

A. Overall, a conservative depreciation approach that considers toll impacts using estimates that are within the range of reasonableness will provide for a reasonable opportunity of generational fairness. When the recommended depreciation parameters as proposed in the current depreciation study were being reviewed, the selection of a specific parameter for each account did consider the ultimate impact on the depreciation expense component of the revenue requirement. In most cases, average service life estimates were lengthened to the long end of the reasonable alternatives, while remaining within an appropriate range. Additionally, the increases in the negative salvage percentages were also moderated to only a level that would represent an estimate at the lower end of the range of reasonable

alternatives. In this manner, the proposed depreciation rates have been developed in a manner that complies with the NARUC guidance and minimizes customer impact while beginning to reverse the historic underfunding of the accumulated depreciation accounts.

Q. DID WITNESS GARRETT UNDERTAKE ANY ANALYSIS OF THE DEPRECIATION PARAMETERS IN HIS TESTIMONY?

A. Mr. Garrett does not describe any substantive analysis of Tennessee American's depreciation study. His Testimony states:

> The Country, including the City Chattanooga and the surrounding communities, has experienced dramatic inflation over the past few years and efforts should be made to restrain further inflation until customer incomes have had a chance to increase. My calculations show that the requested increases in depreciation rates contribute $2.1 million or 16% to the increase in depreciation expense. The recovery of investment costs is a long-term process for public utilities, and there will be time to address any deficiencies in future rate cases when customer earnings are not so heavily stressed.[7]

While customer costs are rising all throughout North America, deferring over $6.3 million of accumulated depreciation deficit to future customers will result in future deficiency that will be even more onerous to the future customers. As noted in this Testimony, the current depreciation rates were approved 17-years ago. Over this 17-year period several social-economic factors have impacted customers over the period where depreciation rates were not adjusted.

Mr. Garrett did not offer any substantive analysis regarding the appropriateness of the depreciation parameters proposed in my depreciation study. There is no regulatory depreciation theory in any textbook, treatise, or other authoritative source that supports Mr.

[7] Garrett Direct Testimony, page 35, lines 4-10.

Garrett's assertion that the depreciation rate should exclude any consideration of the depreciation parameters and instead completely defer the impact of appropriate depreciation parameter recommendations to future customers.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

Tennessee - American Water Company
Summary of Accumulated Depreciation (A/D) Position by Account

Account	Account Name	Calculated A/D	Booked A/D	Deficiency / (Surplus)	% Variance
304.1	Structures & Improvements - Supply	169,236.00	140,879.00	28,357.00	16.76%
304.2	Structures & Improvements - Pumping	2,542,474.00	3,832,463.00	(1,289,989.00)	-50.74%
304.3	Structures & Improrvements - Treatment	3,603,529.00	4,701,594.00	(1,098,065.00)	-30.47%
304.301	Structures & Improvements - Treat-Dpr Paint	1,188,154.00	1,250,689.00	(62,535.00)	-5.26%
304.31	Structures & Improvements - Treatment-Handl	1,011.00	- 42,885.00	43,896.00	4341.84%
304.4	Structures & Improvements - Transmission & Distribution	858,700.00	812,057.00	46,643.00	5.43%
304.5	Structures & Improvements - General	468,798.00	83,282.00	385,516.00	82.23%
304.6	Structures & Improvements - Offices	829,550.00	179,271.00	650,279.00	78.39%
304.7	Structures & Improvements - Store, Shop, Garage	118,871.00	125,768.00	(6,897.00)	-5.80%
304.8	Structures & Improvements - Miscellaneous	198,572.00	494,908.00	(296,336.00)	-149.23%
306	Lake, River & Other Intakes	210,427.00	242,163.00	(31,736.00)	-15.08%
309	Supply Mains	147,333.00	- 229,689.00	377,022.00	255.90%
310	Power Generation Equipment	325,971.00	898,922.00	(572,951.00)	-175.77%
311.2	Pumping Equipment - Electric	2,445,475.00	3,243,080.00	(797,605.00)	-32.62%
311.3	Pumping Equipment - Diesel	57,075.00	71,209.00	(14,134.00)	-24.76%
311.5	Pumping Equipment - Other	519,963.00	- 35,715.00	555,678.00	106.87%
311.52	Pumping Equipment - SOS & Pumping	486,604.00	234,599.00	252,005.00	51.79%
320.1	Water Treatment Equipment - Non-Media	7,013,327.00	5,738,779.00	1,274,548.00	18.17%
320.2	Water Treatment Equipment - Filter Media	1,392,393.00	1,139,350.00	253,043.00	18.17%
330	Distribution Reservoirs & Standpipes	2,515,589.00	1,844,716.00	670,873.00	26.67%
330.003	Tank Repainting	821,703.00	602,567.00	219,136.00	26.67%
330.1	Elevated Tanks & Standpipes	1,331,452.00	976,372.00	355,080.00	26.67%
330.2	Ground Level Tanks	548,534.00	402,248.00	146,286.00	26.67%
330.3	Below Ground Tanks	11,817.00	8,665.00	3,152.00	26.67%
330.4	Clearwell	276,480.00	202,747.00	73,733.00	26.67%
331.001	Transmission & Distribution Mains	48,460,484.00	38,254,119.00	10,206,365.00	21.06%
333	Services	13,313,326.00	10,737,635.00	2,575,691.00	19.35%
334.1	Meters	5,121,189.00	3,714,380.00	1,406,809.00	27.47%
334.11	Meters - Bronze Case	4,145,483.00	5,225,086.00	(1,079,603.00)	-26.04%
334.13	Meters - Other	48,448.00	50,286.00	(1,838.00)	-3.79%
334.131	Meter Reading Units	38,525.00	45,953.00	(7,428.00)	-19.28%
334.2	Meter Installations	7,529,268.00	3,903,027.00	3,626,241.00	48.16%
334.3	Meter Vaults	5,831.00	- 37,344.00	43,175.00	740.44%
335	Hydrants	5,003,165.00	3,728,331.00	1,274,834.00	25.48%
339.2	Other Plant & Equipment - Supply	63,845.00	72,684.00	(8,839.00)	-13.84%
339.6	Other Plant & Equipment - CPS	398,710.00	325,462.00	73,248.00	18.37%
		112,211,312.00	92,937,658.00	19,273,654.00	
340.1	Office Furniture & Equipment	130,414.00	- 33,350.00	163,764.00	125.57%
340.2	Computer & Peripheral Equipment	507,872.00	- 207,861.00	715,733.00	140.93%
340.22	Computer & Peripheral Personal	21,547.00	- 677,356.00	698,903.00	3243.62%
340.23	Computer & Peripheral Other	19,015.00	- 1,077,713.00	1,096,728.00	5767.70%
340.3	Computer Software	4,951,863.00	579,676.00	4,372,187.00	88.29%
340.15	Computer Software Spec Depr Rate	115,983.00	80,992.00	34,991.00	30.17%
340.33	Computer Software Other	422,568.00	82,434.00	340,134.00	80.49%
341.1	Transportation Equipment - Light Duty Trucks	1,371,841.00	3,609,083.00	(2,237,242.00)	-163.08%
341.2	Transportation Equipment - Heavy Duty Trucks	1,469,909.00	3,060,309.00	(1,590,400.00)	-108.20%
341.3	Transportation Equipment - Autos	532,735.00	816,886.00	(284,151.00)	-53.34%
341.4	Transportation Equipment - Other	420,906.00	632,592.00	(211,686.00)	-50.29%
343	Tools, Shop, Garage Equipment	302,867.00	427,355.00	(124,488.00)	-41.10%
344	Laboratory Equipment	31,739.00	16,398.00	15,341.00	48.33%
345	Power Operated Equipment	171,538.00	356,571.00	(185,033.00)	-107.87%
346.1	Communication Equipment - Non-Telephone	133,835.00	51,892.00	81,943.00	61.23%
346.19	Remote Control & Instrument	932,702.00	362,575.00	570,127.00	61.13%
346.2	Communication Equipment - Telephone	4,921.00	- 9,063.00	13,984.00	284.17%
347	Miscellaneous Equipment	221,562.00	56,376.00	165,186.00	74.56%
348	Other Tangible Property	8,109.00	5,016.00	3,093.00	38.14%
		11,771,926.00	8,132,812.00	3,639,114.00	
Total		123,983,238.00	101,070,470.00	22,912,768.00	

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served via U.S. Mail or electronic mail upon:

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This the 22nd day of October 2024.

Melvin J. Malone