STATE OF NEW HAMPSHIRE

BEFORE THE

PUBLIC UTILITIES COMMISSION

DE 16-383

Liberty Utilities (Granite State Electric) Corp. d/b/a Liberty Utilities

Distribution Service Rate Case

DIRECT TESTIMONY

OF

JAMES J. CUNNINGHAM JR.

Date: December 16, 2016

Introduction and Summary

Q. Please state your name, current position and business address.

A. My name is James J. Cunningham Jr. and I am employed by the New Hampshire Public Utilities Commission (Commission) as a Utility Analyst. My business address is 21 S. Fruit Street, Suite 10, Concord New Hampshire, 03301.

Q. Please summarize your educational and professional background.

A. Please see Appendix A.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to provide my recommendations on depreciation and amortization expense and employee pension and benefits expense.

Q. Please summarize your recommendations.

A. Table 1 provides a comparison of the Company's proposed amounts, as updated on November 21, 2016, and my corresponding recommendations.

Table I

Summary of Proposed and Recommended Amounts

	11/21 Upd. Proposed	Recommend	Increase/ (Decrease)
Depreciation & Amortization	$ 5,773,902	$ 5,773,902	$ 0
Employee Pensions & Benefits	$ 4,360,746	$ 3,617,808	$ (742,939)
Total	$10,134,648	$ 9,391,710	$ (742,939)

Schedules supporting my recommended amounts are attached as follows:

Schedule JJC-1, Summary of Recommendations
Schedule JJC-2, Depreciation
Schedule JJC-3, Employee Pensions and Benefits

Q. Are your recommendations reflected in the testimony and schedules of Ms. Mullinax?

A. Yes.

<u>**Depreciation and Amortization**</u>

Q. Please summarize your recommendation for depreciation and amortization.

A. My recommended amount for depreciation and amortization is the same as proposed by the Company – i.e., $5,773,902. The adjustments in this case are limited since Liberty proposes no changes to the existing Commission-approved depreciation accrual rates. Typically, the utilities file a new Depreciation Study if the interval between rate cases is five to ten years; however, in this instant case, only three years has elapsed since the last rate case (i.e., Docket DE 13-063) and a new Depreciation Study is not warranted.

During the course of discovery, there were several adjustments to the plant balances noted; in addition, there were several changes identified in the NHPUC Audit Report. These adjustments resulted in changes to plant account balances as of December 31, 2015, however, the impacts on depreciation expense were generally offsetting.

With respect to non-monetary issues, the NHPUC Audit Report noted that there was an unusually low volume of retirements booked since the previous audit. Liberty concurred that there was a backlog; but, noted that the Company brought in a third plant accountant to assist with the large volume of plant-related transactions, including retirements.[1]

For a summary of depreciation expense by plant account, please refer to Schedule JJC-2.

Q. Were there any changes in the methodology used by Liberty to calculate depreciation expense?

A. No. Liberty uses the whole-life (WL) technique for calculating depreciation rates. The whole-life technique is consistent with the Commission's practice for setting depreciation accrual rates for other electric companies and for natural gas and water utilities.

The WL technique allocates the original cost less the estimated net salvage[2] over the total estimated life of the investment. The WL formula is defined as follows:

$$\text{WL Depreciation Accrual Rate} = \frac{\text{1-Net Salvage Rate (NSR)}}{\text{Average Service Life (ASL)}}$$

For instance, assuming an average service life of 10 years and a net salvage rate of 20 percent, the whole-life depreciation accrual rate is calculated to be 0.08, as follows: 1 - 0.20 / 10 = .08 (or 8.0%).

To the extent that the updated average service lives or net salvage rates turn out to be different than previously estimated, the whole-life technique provides for an amortization of this difference over a short period of time, generally between five to ten years.

[1] Reference: NHPUC Audit Report, November 15, 2016, Audit Issue No. 2, page 82 (attached).
[2] Net salvage represents the estimated gross salvage less the estimated cost of removal at retirement.

Whole-life depreciation accrual rates are easy to administer since the formula is straightforward and the rates remain unchanged until the Commission approves new depreciation accrual rates in subsequent base rate cases.

The WL depreciation accrual rates used by Liberty were authorized by the Commission in Docket No. DE 13-063.[3]

Q. **Liberty provided an updated filing on November 21, 2016. Did the updated filing include any changes to plant balances for purposes of calculating depreciation expense? If yes, please describe the changes.**

A. Yes. Liberty updated depreciation expense to reflect adjustments to plant accounts identified during discovery and during the NHPUC audit.[4] The adjustments pertain mainly to changes in classification. When plant amounts are re-classified, depreciation expense could change since each plant account has a different depreciation accrual rate.

Q. **Please continue by describing the adjustment to plant accounts identified during the course of discovery.**

A. During the course of discovery, it was noted that certain plant balances reported in the Company's 2015 FERC Form-1 were different from the plant balances reflected in the original filing. In its November 21, 2016 correction and update (CU) filing, these differences were reflected. Specifically, Plant Account 365 was increased $105,849 and Plant Account 368 was reduced by $80,950.[5] These adjustments are incorporated in the December 31, 2015 plant balances on the attached Schedule JJC-2, column 1.

---

[3] Reference: Order No. 25,638, March 17, 2014, Settlement Agreement, Attachment C (attached).
[4] Reference: NHPUC Audit Report, November 15, 2016, Audit Issue No. 3 and 7 (attached).
[5] Reference: Staff 3-34 (attached).

Q. Please describe the plant adjustments identified in the NHPUC audit.

A. Certain capital additions were booked to incorrect FERC plant accounts. NHPUC Audit Issue No. 3 recommends that $924,363 be moved from account 396, Power Operated Equipment, to account 392, Transportation Equipment. Since depreciation accrual rates are higher for Transportation Equipment, this adjustment increases depreciation expense by $41,319.[6] Also, there are timing issues – i.e., Audit Issue No. 2 pertains to retirements and recommends that retirements be recorded in a timely manner; and, Audit Issue No. 7 recommends that amounts in CWIP charges be moved to plant account 372 in a timely manner.

Do you have any other comments about balances in the various plant accounts?

A. Yes. With respect to Plant Account 303 Miscellaneous Plant, Liberty correctly made an adjustment to reflect the settlement agreement in Docket No. DG 11-040. This docket pertained to Liberty Utilities' acquisition of Granite State Electric and Energy North Natural Gas. The settlement agreement included a provision that limited the amount of amortization for these IT capital investments. Specifically, the identified capital cost for IT projects was reduced by $6.2 million – i.e., total capital costs identified of approximately $8.6 million reduced to approximately $2.4 million.[7] Liberty's filing as well as my testimony incorporates this adjustment which is shown on the attached Schedule JJC-2, column 3.

---

[6] The depreciation accrual rate for Transportation Equipment is 7.50 percent and the depreciation accrual rate for Power Operated Equipment is 3.03 percent. Therefore, depreciation expense increases by $41,319 (i.e., $924,363 x 4.47 percent).

[7] Reference: For further information about IT amortization, please refer to Staff 1-5 (attached).

Q. The proposed depreciation expense on Schedule RR-3-08 (CU), line 34, includes a reduction in depreciation expense in the amount of $706,686 on line 34. Please explain this adjustment and indicate if you concur with the amount.

A. Yes, I concur with this amount. It pertains to an adjustment that was made as part of the settlement agreement in docket DE 13-063. This adjustment pertains to surplus depreciation reserve amounts that had accumulated at the time of the last depreciation study. To eliminate the surplus reserves, depreciation expense is reduced via an amortization of the surplus depreciation reserves. This amortization credit of $706,686 ends in April 2019.

Q. Please summarize your recommendation for depreciation and amortization expense.

A. Based on the adjustments described above, I recommend depreciation expense of $5,773,902, the same amount as proposed in the November 21, 2016 Update Filing. See attached Schedule JJC-2 for a summary of depreciation expenses by plant account.

<u>Employee Pensions and Benefits</u>

Q. Please begin by summarizing your recommendation for Employee Pensions and Benefits expense.

A. My recommendation for Employee Pensions and Benefits expense is $3,617,808, a reduction of $742,939 from the November 21, 2016 updated proposal amount of

$4,360,746. See attached Schedule JJC-3 for a summary of Employee Pensions and Benefits expense.

Q. Please explain the difference between the proposed amounts and your recommended amount.

A. There are three differences between the proposed amounts and my recommended amounts:

- NHPUC Audit Report adjustment
- Liberty Acquisition Debit amortization
- NEES Acquisition Credit amortization.

Q. Please continue by describing the NHPUC Audit Report adjustment.

A. The Audit Report recommends an adjustment for an overpayment of certain Metlife invoices amounting to $2,047.[8]

Q. You mentioned a second adjustment pertaining to Liberty Acquisition Debit amortization. Please explain this adjustment.

A. The Liberty Acquisition Debit amortization appears in the November 21, 2016 Updated Filing on Schedule RR-3-03, line 38. According to the Technical Statement provided with the November 21, 2016 Update Filing (Item C-1), Liberty will amortize the Liberty Acquisition Debit amortization over 10.52 years, or $2,056,720 per year. I believe this adjustment should be reduced by $689,001.

Q. Please explain why you believe the Liberty Acquisition Debit amortization should be reduced by $689,001.

[8] Reference: NHPUC Audit Report, November 15, 2016, Audit Issue No. 13, page 102 (attached).

A. I believe this amortization should be reduced by capital charges. Liberty makes this adjustment for each of the components of Employee Pensions and Benefits expense – i.e. for Pensions, OPEBs, 401-k, Workers Compensation, Medical and other Health Care costs. That is, each component is reduced by a capital charge of approximately 33.5 percent,[9] except for the Liberty Acquisition Debit amortization.[10] To be consistent with all other components of Employee Pension and Benefits expense, I believe Liberty Acquisition Debit amortization should be reduced by 33.5 percent as well, or $689,001 ($2,056,720 x 33.5%).

Q. In previous years, did Liberty make the adjustment for the capital charge related to the Liberty Acquisition Debit amortization?

A. Yes. Staff analysis indicates that the capital charge was applied to the Liberty Acquisition Debit amortization in the 2015 test year. The gross amount of Liberty Acquisition Debit amortization was $2,014,135 and the capital charge was $961,547, with the remaining amount of $1,052,588 charged to operations.[11]

Q. You mentioned above that you recommend a third adjustment pertaining to the NEES acquisition Credit amortization. Please explain this adjustment.

A. Liberty's November 21, 2016 Update Filing, Schedule RR-3-03, line 37, indicates that the amortization of the NEES Acquisition Credit expires in 2016. Staff analysis indicates that the NEES Acquisition Credit has a number of components, and each one is amortized over a different period of time. It appears that one component is not yet fully amortized and will not be fully amortized until January

---

[9] Reference: Original filing, Schedule RR-3-03, line 6, Bates 145; $225,338 / $672,729 = 33.5 percent.
[10] Reference: November 21, 2016 Update Filing, RR-3-03, line 38 (Bates 29).
[11] Reference: Staff 9-12 (attached). The attachment to this response, at line 8, indicates that the capitalized portion of additional pension amortization (i.e., Liberty Acquisition Debit amortization) is $961,547.

2018. The annual credit amortization for 2016 for this particular component is $78,031.[12]

Q. Do you recommend that the NEES Acquisition Credit amortization be reduced by a capital charge, similar to the other components of Employee Pension and Benefit expenses?

A. Yes. Based on a capital charge of 33.5 percent, I recommend that NEES Acquisition Credit amortization of $78,031 be reduced by $26,140, leaving a remaining Credit amortization of $51,891.

Q. Please summarize your recommendation for Employee Pension and Benefit expenses.

A. My recommendation for Employee Pension and Benefit expenses is $3,617,808, a reduction of $742,939 from the proposed amount of $4,360,746. See attached Schedule JJC-3 for a summary of Employee Pensions and Benefits expenses. Also see attached Work paper JJC-3.1 for additional detail on the derivation of these adjustments.

Q. Does that complete your testimony?

A. Yes it does, thank you.

---

[12] Reference: Staff Testimony in DE 13-063, Staff 3-33 (attached).