**FLORIDA PUBLIC SERVICE COMMISSION**

 **Fletcher Building**

 **101 East Gaines Street**

 **Tallahassee, Florida 32399-0850**

 **M E M O R A N D U M**

 **March 4, 1993**

**TO : DIRECTOR OF RECORDS AND REPORTING**

**FROM : DIVISION OF AUDITING AND FINANCIAL ANALYSIS (MEEKS, HICKS)**

 **DIVISION OF LEGAL SERVICES (KURLIN)**

**RE : DOCKET NO. 920823-TL, FLORALA TELEPHONE CO., INC. – 1992**

 **DEPRECIATION STUDY**

**AGENDA : MARCH 16, 1993 - PROPOSED AGENCY ACTION – CONTROVERSIAL**

* **PARTIES MAY PARTICIPATE**

**CRITICAL DATES: NONE**

**SPECIAL INSTRUCTIONS: I:\PSC\AFA\WP\920823.RCM**

 **R:FLORALA1.WK3**

 **DISCUSSION OF ISSUES**

**ISSUE :** Should the current depreciation rates and recovery schedules for Florala Telephone Co., Inc. (Florala or Company) be changed?

**RECOMMENDATION:** Yes. A review of Company plans and the status of life, salvage and reserve parameters presented in the study indicate the need for a revision of depreciation rates. (MEEKS)

**STAFF ANALYSIS:** Florala Telephone Co., Inc. currently operates with remaining life rates and recovery schedules approved by the Commission effective January 1, 1990. Since the time of that represcription, the Company's eletromechanical switches have been retired and replaced by two digital switches. The unrecovered investment of these retired switches and associated circuit equipment were placed on recovery schedules as part of the last review. These schedules are now complete.

 A review of Florala's plans indicate that no new recovery schedules are required at this time. Growth in the Laurel Hill area has prompted placement of a new toll route with the Company's first fiber cable application together with the associated optical circuit equipment. Further, as several accounts have experienced a high degree of activity, the updated remaining lives, resultant plant and reserve balances should be incorporated in revised remaining life rates. The depreciation rates should therefore be revised at this time.

**ISSUE 2:** What should be the date of implementation for new rates?

**RECOMMENDATION**: Staff recommends approval of Florala's proposed January 1, 1993 date of implementation for the new depreciation rates. (MEEKS)

**STAFF ANALYSIS:** Company data submitted and related calculations abut the January 1, 1993 date. This is the recommended date of implementation, being the earliest practicable date for utilizing the revised rates.

**ISSUE 3:** Should any corrective reserve transfers be made?

**RECOMMENDATION**: Yes, staff recommends that the corrective reserve measures as shown on Attachment A, page 8, be made. (MEEKS)

**STAFF ANALYSIS:** As part of Docket No. 861151-TL, recovery was provided for the net unrecovered investment associated with analog circuit equipment, which was expected to retire in 1989. The retirement of this equipment was completed in 1990. There is now a reserve surplus of $30,696 associated with this retirement primarily due to an unexpected need in the Alabama operations for this equipment. The Company has proposed to transfer this surplus to the current Circuit-Analog depreciable category. Staff recommends acceptance of this proposal which will more than offset the perceived reserve deficit in this account. A review of the current reserve position for each account indicates that no other reserve transfers are necessary at this time.

**ISSUE 4:** What are the appropriate lives, net salvages, reserves and resultant depreciation rates for each account?

**RECOMMENDATION:** The Staff recommended lives, net salvages, reserves and resultant depreciation rates are shown on Attachment B, page 9. This results in an increase in annual depreciation expense of approximately $38,000 based on January 1, 1993 investments as shown on Attachment C, page 10. (MEEKS)

**STAFF ANALYSIS:** The staff recommendations are the result of a comprehensive review of the Company's depreciation study. Attachment B, page 9, shows a comparison of the currently approved, Company proposed, and staff recommended rate parameters (lives, salvages, and reserves). Attachment C, page 10, shows a comparison of resultant expenses based on January 1, 1993 investments. For the most part, the Company proposed life and salvage parameters are reasonable and in line with current industry projections. The major differences between the Company's position and the staff are discussed below.

Information Origination/Termination Equipment-Paystations. While staff accepts the Company's life proposal, the salvage factor is apparently based on the fact that salvage was booked in only one year of activity (1989) which resulted in a negative 1% net salvage. It is also noted that this account only shows two retirements since 1985. With such a small universe and relatively no activity, staff recommends retention of the current salvage factor of zero at this time.

Poles. Staff accepts the life parameters for this account but believes that a (40)% future net salvage factor is more representative of the future than the Company's proposal to retain the currently prescribed (15)% factor. This is a labor sensitive account and as noted in the Company's study, future reuse salvage is not expected to be a factor in this account. In its response to the staff report, the (40)% is acceptable to the Company.

Underground Cable-Metallic. Staff accepts the life parameters for this account but believes that the Company's proposal of zero future net salvage is not representative of the future. Most of this investment will be abandoned in place upon retirement. However, taking into consideration that some associated equipment such as pedestals are physically removed, staff recommends the use of negative five percent future net salvage to recognize these removal costs. The Company has concurred in this recommendation in its response to the staff report.

**ISSUE 5:** Should the current amortization of investment tax credits (ITCs) and the flowback of excess deferred income taxes be changed to reflect the new depreciation rates and recovery schedules?

**RECOMMENDATION:** Yes. The current amortization of investment tax credits (ITCs) and the flowback of excess deferred income taxes should be changed to reflect the new depreciation rates and recovery schedules. (HICKS)

**STAFF ANALYSIS:** During staff's review of Florala Telephone's depreciation study, staff discovered that the utility did not change its amortization of ITCs and excess deferred income taxes with each depreciation represcription. Investment tax credits, according to Florala, are amortized using the remaining asset lives in effect at the time the credits were generated. Likewise, the excess deferred income taxes are amortized using the remaining asset lives in effect at the time the Commission began requiring the amortization of excess deferred income taxes. Staff believes that the amortization of ITCs and excess deferred income taxes should be changed with each subsequent depreciation represcription.

 Section 46(f), Internal Revenue Code states that the amortization of ITCs should be determined by the period of time used in computing depreciation expense for purposes of reflecting operating results of the utility. Staff believes that the amortization of excess deferred income taxes should be determined in the same manner for consistency purposes.

 Staff recommends that Florala be required to amortize ITCs and excess deferred income taxes over the remaining life of the assets which generated them. The change in amortization should be on a prospective basis and reflected in its surveillance reports.

**ISSUE 6:** Should this docket be closed?

**RECOMMENDATION:** Yes, assuming no objections to the Proposed Agency Action Order are filed. (MEEKS)

**STAFF ANALYSIS:** In staff's opinion, no further Commission action is necessary if no objections to the PAA Order are filed.

 FLORALA TELEPHONE CO., INC.‑FLORIDA

 1992 STUDY

 RECOMMENDED RESERVE TRANSFERS

 1‑1‑93

 ESTIMATED RESTATED

 ACCOUNT BOOK RESERVE TRANSFERS RESERVE

 ($) ($) ($)

 CIRCUIT‑ANALOG 30,696 (30,696) ‑0‑

 RECOVERY SCHEDULE

 CIRCUIT‑ANALOG 17,083 30,696 47,779

 DEPRECIABLE ASSETS

 TOTALS 47,779 ‑0‑ 47,779

 FLORALA TELEPHONE CO., INC. ‑ FLORIDA

 1992 STUDY

 COMPARISON OF RATES AND COMPONENTS

 CURRENT COMPANY PROPOSAL STAFF RECOMMENDATION

 AVERAGE REMAINING AVERAGE REMAINING AVERAGE REMAINING

 REMAINING NET LIFE REMAINING NET LIFE REMAINING NET LIFE

ACCOUNT LIFE SALVAGE RESERVE RATE LIFE SALVAGE RESERVE RATE LIFE SALVAGE RESERVE RATE

 (YRS.) (%) (%) (%) (YRS.) (%) (%) (%) (YRS.) (%) (%) (%)

**GENERAL SUPPORT ASSETS**

 Buildings 23.0 0.0 33.66 2.9 19.8 0.0 41.81 2.9 19.8 0.0 41.81 2.9

**CENTRAL OFFICE ASSETS**

 Digital ESS 15.5 5.0 0.00 6.1 \* 14.6 5.0 7.10 6.0 14.6 5.0 7.10 6.0

 Circuit ‑ Analog 10.0 0.0 0.00 10.0 \* 5.1 0.0 88.78 \*\* 2.2 5.1 0.0 88.78 \*\* 2.2

 Circuit ‑ Digital 10.2 0.0 15.01 8.3 7.8 0.0 40.00 7.7 7.8 0.0 40.00 7.7

 Circuit ‑ Digital Cap. Rec. Sch. 100.00 100.00

 Circuit ‑ Optical Eqpt. 10.0 0.0 0.00 10.0 \* 10.0 0.0 0.00 10.0 \* 10.0 0.0 0.00 10.0 \*

**INFORMATION ORIG/TERM ASSETS**

 Info Orig. Term. 6.1 0.0 40.61 9.7 4.9 (1.0) 60.18 8.3 4.9 0.0 60.18 8.1

**CABLE & WIRE FACILITIES**

 Poles 12.4 (15.0) 54.99 4.8 11.4 (15.0) 65.95 4.3 11.4 (40.0) 65.95 6.5

 Aerial Cable ‑ Metallic 14.6 (15.0) 43.14 4.9 10.2 (15.0) 53.57 6.0 10.2 (15.0) 53.57 6.0

 Aerial Cable ‑ Fiber 20.0 0.0 0.00 5.0 \* 20.0 (15.0) 0.00 5.8 \* 20.0 (15.0) 0.00 5.8 \*

 Undgd. Cable ‑ Metallic 12.0 0.0 43.72 4.7 11.0 0.0 57.86 3.8 11.0 (5.0) 57.86 4.3

 Undgd. Cable ‑ Fiber 20.0 0.0 0.00 5.0 \* 20.0 (5.0) 0.00 5.3 \* 20.0 (5.0) 0.00 5.3 \*

 Buried Cable ‑ Metallic 16.8 (5.0) 22.66 4.9 11.9 (5.0) 27.86 6.5 11.9 (5.0) 27.86 6.5

 Buried Cable ‑ Fiber 20.0 0.0 0.00 5.0 \* 20.0 (5.0) 0.00 5.3 \* 20.0 (5.0) 0.00 5.3 \*

 Conduit 43.0 (4.0) 12.03 2.1 41.0 (4.0) 16.04 2.1 41.0 (4.0) 16.04 2.1

 \*Denotes Whole Life Rate

 \*\*Denotes restated reserve

 FLORALA TELEPHONE CO., INC. ‑ FLORIDA

 1992 STUDY

 COMPARISON OF EXPENSES

 CURRENT COMPANY PROPOSAL STAFF RECOMMENDATION

 CHANGE CHANGE

 1/1/93 1/1/93 IN IN

ACCOUNT INVESTMENT RESERVE RATE EXPENSES RATE EXPENSES EXPENSES RATE EXPENSES EXPENSES

 ($) ($) (%) ($) (%) ($) ($) (%) ($) ($)

**GENERAL SUPPORT ASSETS**

 Buildings 75,030 31,368 2.9 2,176 2.9 2,176 0 2.9 2,176 0

 Subtotal 75,030 31,368 2,176 2,176 0 2,176 0

**CENTRAL OFFICE ASSETS**

 Digital ESS 837,127 59,424 6.1 51,065 6.0 50,228 (837) 6.0 50,228 (837)

 Circuit‑Analog 53,820 47,779 \*\* 10.0 5,382 2.2 1,184 (4,198) 2.2 1,184 (4,198)

 Circuit ‑ Digital 500,095 200,016 8.3 41,508 7.7 38,507 (3,001) 7.7 38,507 (3,001)

 Circuit‑Digital Cap. Rec. Sch. 5,227 5,227

 Circuit ‑ Optical Eqpt. 0 0 10.0 \* 0 10.0 \* 0 0 10.0 \* 0 0

 Subtotal 1,396,269 312,446 97,955 89,919 (8,036) 89,919 (8,036)

**INFORMATION ORIG/TERM ASSETS**

 Info Orig. Term. 8,058 4,849 9.7 782 8.3 669 (113) 8.1 653 (129)

 Subtotal 8,058 4,849 782 669 (113) 653 (129)

**CABLE & WIRE FACILITIES**

 Poles 68,852 45,409 4.8 3,305 4.3 2,961 (344) 6.5 4,475 1,170

 Aerial Cable ‑ Metallic 75,658 40,527 4.9 3,707 6.0 4,539 832 6.0 4,539 832

 Aerial Cable ‑ Fiber 0 0 5.0 \* 0 5.8 \* 0 0 5.8 \* 0 0

 Undgd. Cable ‑ Metallic 2,086 1,207 4.7 98 3.8 79 (19) 4.3 90 (8)

 Undgd. Cable ‑ Fiber 0 0 5.0 \* 0 5.3 \* 0 0 5.3 \* 0 0

 Buried Cable ‑ Metallic 2,760,059 768,891 4.9 135,243 6.5 179,404 44,161 6.5 179,404 44,161

 Buried Cable ‑ Fiber 0 0 5.0 \* 0 5.3 \* 0 0 5.3 \* 0 0

 Conduit 90,563 14,529 2.1 1,902 2.1 1,902 0 2.1 1,902 0

 Subtotal 2,997,218 870,563 144,255 188,885 44,630 190,410 46,155

 GRAND TOTAL 4,476,575 1,219,226 245,168 281,649 36,481 283,158 37,990

 \*Denotes Whole Life Rate

 \*\*Denotes restated reserve