State of Florida

Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

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

DATE: SEPTEMBER 4, 2003

TO: DIRECTOR, DIVISION OF THE COMMISSION CLERK & ADMINISTRATIVE SERVICES (BAYÓ)

FROM: DIVISION OF ECONOMIC REGULATION (P. LEE) Pay from Todd
DIVISION OF AUDIT & SAFETY (MILLS) Curt
OFFICE OF THE GENERAL COUNSEL (JAEGER) Matt

RE: DOCKET NO. 030048-GU - 2003 DEPRECIATION STUDY FOR INDIANTOWN GAS COMPANY.

AGENDA: 09/16/03 - REGULAR AGENDA - PROPOSED AGENCY ACTION - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\ECR\WP\030048.RCM

CASE BACKGROUND

Rule 25-7.045, Florida Administrative Code (F.A.C.), requires gas companies to file comprehensive depreciation studies at least once every five years. On January 14, 2003, Indiantown Gas Company, Inc. (IGC or company) filed its regular depreciation study in accordance with this rule. IGC's last comprehensive depreciation study was filed on July 9, 1998. Staff has completed its review of this study and presents its recommendation herein.

The Commission has jurisdiction in this matter pursuant to Sections 366.04, 366.05, and 366.06, Florida Statutes.

DISCUSSION OF ISSUES

ISSUE 1: Should the current depreciation rates for Indiantown Gas Company, Inc. be changed?

RECOMMENDATION: Yes. A review of the company's current capital recovery position indicates the need to revise the current prescribed depreciation rates. (P. LEE)

STAFF ANALYSIS: IGC filed its last depreciation study in 1998 with an effective date for revised depreciation rates of January 1, 1998. Under Rule 25-7.045 (8), F.A.C., gas companies are required to file a comprehensive depreciation study at least once every five years. Changes since the last study brought about by activity and company planning indicate the need to revise currently prescribed depreciation rates.

ISSUE 2: What should be the date of implementation for revised depreciation rates and capital recovery schedules?

RECOMMENDATION: Staff recommends approval of the company's proposed January 1, 2003, date of implementation for revised depreciation rates and recovery schedules. (P. LEE)

STAFF ANALYSIS: The company proposed January 1, 2003, implementation date for revised depreciation rates and recovery schedules matches the beginning of its fiscal year. In keeping with Rule 25-7.045(6), F.A.C., all data and related calculations have been provided coinciding with the proposed date. Staff therefore recommends approval of a January 1, 2003, implementation date.

ISSUE 3: Should any corrective reserve measures be made?

RECOMMENDATION: Yes. Staff recommends the following corrective measures be made to the reserve:

Account	Book Reserve	Recommended Transfers	Restated Reserve
	($)	($)	($)
376 - Mains - Steel	151,849	85,637	237,486
376 - Mains - Plastic	156,530	(85,637)	70,893
380 - Services - Plastic	30,599	(9,586)	21,013
378 - M&R Equip. - General	(1,958)	9,586	7,628
391 - Office Furniture	10,378	(6,906)	3,472
Computer Equipment	13,211	6,906	20,117
392 - Transportation Equipment	85,084	(2,486)	82,598
397 - Communication Equipment	(1,416)	2,486	1,070
Total	444,277	0	444,277

(P. LEE)

STAFF ANALYSIS: As part of staff's review of IGC's depreciation study, a review of the reserve position for each account was performed. The Commission's approach to reserve transfers is where surpluses and deficits exist, corrective reserve transfers between accounts should be considered.

Since the 1998 study, about 64% of the Measuring & Regulating (M&R) station equipment - General investment (Account 378) has retired. The retirements related to two regulator stations and the company's original odorizer. The odorizer was actually replaced in 1993 but the retirement was overlooked until 1999. These retirements were not foreseen in the currently prescribed depreciation rate design. As a consequence, the account reserve is now negative. The negative reserve relates to plant no longer providing service and should be corrected as soon as possible. Moreover, $4,745 was transferred from M&R Equipment - Industrial (Account 385) to M&R Equipment - General (Account 378) in 1999 without any commensurate reserve being transferred. According to IGC's continuing property records, the transferred investment was

placed in service in 1981. Thus, at the time of the transfer, the associated reserve was $3,160 ($4,745 * 3.6% * 18.5 yrs.). Staff recommends a corrective transfer of $9,586 from the reserve surplus existing in Account 380, Plastic Services, to Account 378 to correct the existing reserve deficiency.

As a result of a physical inventory, IGC found that $4,373 in computer equipment reflected on the books of the company were no longer in service. After the inventory adjustment, staff recommends a transfer of $6,906 from the calculated surplus existing in Office Furniture, Account 391, to bring the computer equipment reserve to its theoretically correct level.

The Communication equipment (Account 397) experienced a retirement of $1,502 in 2000 that represented four two-way radios. The equipment was only 3.5 years old at the time of retirement. Such activity was unforeseen in the design of the currently prescribed depreciation rate. Staff recommends a reserve transfer from the existing surplus in Transportation equipment, Account 392, to correct the reserve deficiency in communication equipment.

In light of the possible impact of reserve transfers on cost allocations, the company should make corresponding entries to the related depreciation expense accounts for the reserve transfers discussed above.

ISSUE 4: What are the appropriate depreciation rates and recovery schedules for IGC?

RECOMMENDATION: The staff recommended remaining lives, net salvage values, reserve positions, and resultant depreciation rates and recovery schedules are shown on Attachment A. These recommendations result in a decrease in annual depreciation expense of about $1,500, based on January 1, 2003, investments and reserves as shown on Attachment B. (P. LEE)

STAFF ANALYSIS: Staff's recommendations are the result of a comprehensive review of IGC's submitted data and information. This filing was essentially a staff-assisted study. The company provided the necessary data for staff to develop an average age for each account's surviving investment as of January 1, 2003. Staff and the company then worked together in developing appropriate life and salvage values.

IGC operates in a stable community, which has been generally reflected by the lack of additions and retirements. During the 1993-2003 period, IGC experienced significant growth while retirements remained infrequent. The growth was attributed to the addition of a second industrial customer, the US Generating Cogeneration facility, and a system upgrade. Over the past several years, the company has been replacing its 3/4-inch steel mains with 1.25-inch plastic. This upgrade program also involves the replacement of the service line riser, and new meter and regulator sets. The time table for the mains replacement project has been modified, although the overall retirement goals remain the same. The project has been suspended for the duration of 2003 and is expected to resume mid-year 2004 with expected completion December 31, 2005.

The expected average service life for each account is estimated from an analysis of historic activity, expected impact of factors such as growth and technological change, and industry averages. Staff's review of each account's activity indicates that changes in the average service life for one account and in the net salvage values for several accounts are warranted. The company's continuing property record (CPR) system has been used to develop the current average age of surviving investment for each account. The recommended remaining lives reflect CPR data and activity since the last study.

As a result of the review and analytical process, IGC has agreed with staff on life and salvage values for each account. The recommended depreciation rates and recovery schedules can be attributed mainly to three factors - updated ages to reflect activity since the last represcription, changes in the reserve position, and revised net salvage values.

Distribution Plant

Mains replacement program

In 1993 and 1994, IGC began renovations to a six-inch gas main to comply with the Department of Transportation requirements for a road construction project and to update the system pressure to accommodate the US Generating Cogeneration facility. Additionally, the company began upgrading its system by replacing all 3/4 inch steel mains with 1.25 inch plastic mains. This project also involves replacement of IGC's steel service lines, risers, meters, and regulators. The project has been temporarily suspended for the duration of 2003 and is expected to resume mid-year 2004. Current planning is for the upgrade to be completed by year-end 2005.

At the time of the 1998 depreciation review, the mains replacement project was expected to be completed by year-end 2000. A recovery schedule designed to recover the associated net investments estimated to be replaced as part of the upgrade program was established. The unrecovered investments were estimated as $14,148 and were to be amortized over three years coinciding with completion of the program. The net investments included a 30 percent allowance for expected removal costs for the retiring mains. It was anticipated that any necessary true-up would be made at the time of the 2003 prescription.

With the revision in the program completion date from year-end 2000 to year-end 2005, the investments subject to retirement are recovered. No further recovery is needed. In the event that the expected cost of removal is not incurred, any reserve surplus remaining at the completion of the project can be addressed as part of the company's next depreciation review.

As a result of the renovations and upgrades, significant additions have been made in Industrial Measuring and Regulating Equipment, Account 384; Plastic Services, Account 380; Meters and Regulators, Accounts 381 and 383; and, Meter and Regulator

Installations, Accounts 382 and 384. These additions translate into a younger average age for the related investments, thus a longer remaining life than last prescribed.

Mains and Services

Mains and services comprise about 72 percent of the investment in the distribution plant function. As a result of the mains replacement program, all steel services are being replaced with plastic services. Additionally, mains and services have experienced an eight percent growth since the 1998 review.

Mains and service lines are generally abandoned in place upon retirement. This involves travel time for the crew, digging down to the main or service, cutting and capping, refilling the hole, and restoring the roadway. Restoring the roadway can become significant if the lines are under pavement. Surface restoration normally occurs at two locations for each service line retired; one at the point of the service riser, and the other at the property line or at the connection to the main. The galvanic action of dissimilar metals such as a galvanized steel service line running off a cast iron main requires that the line be cut at the main rather than the property line. Under these circumstances, paving restoration is required.

According to IGC, travel to any location within its service territory is only five minutes and the majority of its mains and services are located on easements, not under pavement. Generally, when a main or service line is replaced, the new pipe is placed in the same trench parallel to the existing pipe. In other words, a single trench is dug in which the existing main or service is cut and capped, and the new pipe is placed next to the abandoned pipe. According to IGC, the labor is not segregated between new installations and the cost of abandoning the retired installation. The associated labor cost of abandoning the retired main or service is included with the capitalized cost of the new installation. This approach understates the cost of removing the old pipe and overstates the capitalized new addition. In cases as this where the labor to abandon the existing main is not easily separated from the cost of the new installation, the cost of trenching and travel should be equitably allocated between the cost of abandoning the old and installing the new. A suggested approach would be to record the labor involved with digging the trench and cutting and capping as cost of removal associated with the retiring

installation and the labor involved with installing the new line and filling in the trench as part of the capital addition of the new pipe. Whether the company uses this approach or some other, there needs to be equitable recognition that there are costs associated with the abandonment of the existing installation.

The recommended remaining lives for these accounts simply reflect an update of each account's age to reflect activity since the last study. The recommended net salvage values are based on expectations of other gas companies in the state and assume that labor costs are equitably allocated between abandoning an existing installation and placing a new main or service line.

Measuring and Regulating Station Equipment-General (Account 378)

This account consists of regulators and other equipment used to maintain the correct operating pressure throughout the distribution system. Two regulator installations and an odorizer comprising about 64 percent of the account's investment retired in 1999. Reserve transfers recommended in Issue 3 will correct the resulting reserve deficiency. The recommended average remaining life simply reflects an update of the account's age since the last study. No change in the currently prescribed zero net salvage is warranted.

Meters and Regulators (Accounts 381 and 383)

Meters are used to measure gas consumption at the customer's premise; regulators are used to regulate the gas pressure at the customer's premise. Under Rule 25-7.0461(6), F.A.C., the accounting treatment for this equipment is cradle-to-grave. At the time a meter or regulator is purchased, the cost is capitalized. A retirement does not occur until final disposition. All costs associated with change-outs and refurbishment are expensed. There is nothing in the current filing to indicate the need for a change in average service lives or net salvage values for these accounts. The recommended remaining lives reflect an update of each account's age since the last depreciation review.

Meter and Regulator Installations (Accounts 382 and 384)

According to the company, installation costs associated with house regulators are recorded along with the meter installation costs due to the minimal cost per installation. When a meter or

regulator is placed in a location which has never before had service, or when an additional meter or regulator is added to an old location (increasing the number at the location), the installation costs are capitalized. Generally, meter and regulator installations are retired only when the meter or regulator is removed from the location and no new one is installed, or when service through the meter or regulator is cut. In other words, the life of these installations should be very similar to the life of services.

Sixty-eight percent of the January 1, 2003 meter and regulator investment represents plant added in the last four years. This growth is primarily associated with the ongoing mains upgrade program. The recommended average remaining life is the result of updating the account age to reflect activity since the last represcription. The recommended negative five percent net salvage recognizes labor associated with the removal of these installations.

General Plant

Structures and Improvements (Account 390)

The investment in this account represents the company office building and remodeling improvements. The remodeling improvements largely took place in 2000 and represent the bulk of the investment. A 40-year average service life is recommended as being in the range of expectations for this account as seen from other gas companies in the state. No change in the currently prescribed zero net salvage is indicated.

Office Furniture and Computer Equipment (Account 391)

Since the 1998 depreciation review, the company has performed a physical inventory of its office furniture and computer equipment. As a result, the office furniture investment is reduced by $32,417 to reconcile IGC's general ledger with its CPRs; the computer investment is reduced by $4,373. The investments and reserves shown on Attachment B reflect these inventory adjustments. The recommended remaining lives simply reflect an update for the current average ages.

Transportation Equipment (Account 392)

A review of the account's activity indicates that IGC's vehicles retire at an average age of about six years, in line with the average service life underlying the currently prescribed average remaining life. The average remaining life reflects an update for the average age of the surviving investment. A ten percent net salvage provides some recognition of resale or trade-in value upon retirement.

Power Operated Equipment

The investment in this account reflects the cost of a mini-trackhoe designed to excavate in small areas such as easements and back yards. It was leased throughout 1996 and then purchased in December 1996. The recommended average remaining life reflects the current average age of the investment. The zero net salvage value reflects the expectation of little if any gross salvage, offset by attendant costs of retirement.

Communication Equipment

Since the last depreciation review, the company retired its four two-way radios and installed a phone system in 2000. The recommended average remaining life and net salvage value reflect the current average age of the surviving investment and recognizes that this equipment is subject to technological impacts.

ISSUE 5: Should this docket be closed?

RECOMMENDATION: If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, this docket should be closed upon the issuance of a consummating order. (JAEGER)

STAFF ANALYSIS: If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, this docket should be closed upon the issuance of a consummating order.

Attachment A

INDIANTOWN GAS COMPANY
2003 STUDY
COMPARISON OF RATES AND COMPONENTS

ACCOUNT		CURRENT				STAFF/COMPANY RECOMMENDED				
		AVERAGE REMAINING LIFE (YRS.)	NET SALVAGE (%)	REMAINING LIFE RATE (%)		AVERAGE REMAINING LIFE (YRS.)	NET SALVAGE (%)	1/1/03 RESERVE (%)	REMAINING LIFE RATE (%)	
GAS DISTRIBUTION										
376	Mains - Steel	19.6	(30.0)	3.1		14.0	(30.0)	71.47	4.2	
376	Mains - Plastic	19.0	(30.0)	3.0		23.0	(30.0)	54.10	3.3	
378	M&R Equipment - General	15.3	0.0	2.0		29.0	0.0	2.51 **	3.4	
380	Services - Steel	17.4	(35.0)	3.2				NA		
380	Services - Plastic	16.0	(35.0)	3.5		25.0	(35.0)	52.22	3.3	
381	Meters	13.1	0.0	1.6		13.9	0.0	47.24	3.8	
382	Meter Installations	23.0	(5.0)	1.5		32.0	(5.0)	22.69	2.6	
383	House Regulators	16.7	0.0	2.0		20.0	0.0	39.31	3.0	
384	House Regulators - Installations	23.0	0.0	1.0				NA		
385	M&R Equipment - Industrial	11.9	0.0	2.8		16.8	0.0	40.73 **	3.5	
387	Other Equipment	25.0	0.0	4.0		25.0	0.0	0.00	4.0	*
GENERAL PLANT										
390	Structures & Improvements	31.0	0.0	3.2	*	36.0	0.0	10.45	2.5	
391	Office Furniture	20.0	0.0	6.0	*	17.5	0.0	12.50 **	5.0	
	Computer Equipment	5.6	0.0	1.2		3.3	0.0	57.37 **	12.9	
392	Transportation Equipment	6.0	10.0	15.0	*	2.6	10.0	51.52 **	14.8	
394	Tools, Shop, and Garage Equip.	17.0	0.0	4.9		13.9	0.0	29.23	5.1	
396	Power Operated Equipment	13.5	0.0	6.7		8.5	0.0	43.61	6.6	
397	Communication Equipment	11.5	0.0	8.4		8.5	0.0	29.45 **	8.3	
RECOVERY SCHEDULES										
	Main and Service Replacement Project	3 Year Amortization				2 Year Remaining Amortization				

* Denotes whole life rate.
** Denotes restated reserve after corrective measures.

Attachment B

INDIANTOWN GAS COMPANY
2003 STUDY
COMPARISON OF EXPENSES

	ACCOUNT	INVESTMENT 1/1/2003 ($)		RESERVE 1/1/2003 ($)		CURRENT RATE (%)		CURRENT EXPENSES ($)	STAFF/COMPANY RECOMMENDED RATE %		STAFF/COMPANY RECOMMENDED EXPENSES $	CHANGE IN EXPENSES $
GAS DISTRIBUTION												
376	Mains - Steel	332,266		237,486	**	3.1		10,300	3.1		10,300	0
376	Mains - Plastic	131,040		70,893	**	3.0		3,931	2.6		3,407	(524)
378	M&R Equipment - General	47,973		1,202	**	2.0		959	2.9		1,391	432
380	Services - Steel	0		0		3.2		0			NA	
380	Services - Plastic	58,591		21,013		3.5		2,051	3.2		1,875	(176)
381	Meters	37,244		17,595		1.6		596	3.8		1,415	819
382	Meter Installations	6,255		1,419		1.5		94	2.6		163	69
383	House Regulators	11,287		4,437		2.0		226	3.0		339	113
384	House Regulators - Installations	0		0		1.0		0			NA	
385	M&R Equipment - Industrial	98,377		40,069	**	2.8		2,755	3.3		3,246	491
387	Other Equipment	0		0		4.0	*	0	4.0	*	0	0
	Total Distribution	723,033		394,114				20,912			22,136	1,224
GENERAL PLANT												
390.0	Structures & Improvements	171,895		17,956		3.2		5,501	2.5		4,297	(1,204)
391	Office Furniture	27,774		3,472	**	5.0	*	1,389	5.0		1,389	0
	Computer Equipment	27,445		15,744	**	1.2	•	329	12.9		3,540	3,211
392.0	Transportation Equipment	165,559		82,598	**	15.0		24,834	14.8		24,503	(331)
394.0	Tools, Shop, and Garage Equip.	5,925		1,918		4.9	•	290	5.1		302	12
396.0	Power Operated Equipment	9,824		4,284		6.7		658	6.6		648	(10)
397.0	Communication Equipment	3,633		1,070	**	8.4		305	8.3		302	(3)
	Total General Plant	412,055		127,042				33,306			34,981	1,675
RECOVERY SCHEDULES												
	Main and Service Replacement Project	19,354		21,905		3-YR.AMORT.		4,415	2-YR. AMORT.		0	(4,415)
	TOTAL PLANT	1,154,442		543,061				58,633			57,117	(1,516)

• Denotes whole life rate.
** Denotes restated reserve after corrective measures.