

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Request for approval of  
change in depreciation rates to  
be implemented as of 10/1/03, by  
City Gas Company of Florida.

DOCKET NO. 030222-GU  
ORDER NO. PSC-03-1147-PAA-GU  
ISSUED: October 14, 2003

The following Commissioners participated in the disposition of  
this matter:

LILA A. JABER, Chairman  
J. TERRY DEASON  
BRAULIO L. BAEZ  
RUDOLPH "RUDY" BRADLEY  
CHARLES M. DAVIDSON

NOTICE OF PROPOSED AGENCY ACTION ORDER REQUIRING  
CORRECTIVE RESERVE TRANSFERS, REVISING DEPRECIATION RATES,  
AND REQUIRING FILING OF DETAILED CALCULATIONS SHOWING  
REVISIONS OF INVESTMENT TAX CREDITS AMORTIZATION AND  
FLOWBACKS OF EXCESS DEFERRED INCOME TAXES

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service  
Commission that the action discussed herein is preliminary in  
nature and will become final unless a person whose interests are  
substantially affected files a petition for a formal proceeding,  
pursuant to Rule 25-22.029, Florida Administrative Code.

I. BACKGROUND

Rule 25-7.045, Florida Administrative Code (F.A.C.), requires  
gas utilities to file comprehensive depreciation studies at least  
once every five years. On March 4, 2003, City Gas Company of  
Florida (City Gas or company) filed its regular depreciation study  
in accordance with this rule. The last comprehensive depreciation  
re prescription for City Gas was made in 1999.

DOCUMENT NUMBER DATE

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FPSC-COMMUNICATIONS

We have jurisdiction in this matter pursuant to Sections 366.04, 366.05, and 366.06, Florida Statutes.

## II. IMPLEMENTATION DATE FOR NEW RATES

A review of the company's current capital recovery position, shows that since the company's 1999 study, Phase 1 of the East/West pipeline has been completed. Two customers, Florida Crystals and Wackenhut Prison, are currently being served by the new pipeline with several other parties and industrial projects under development along the pipeline route.

In 1999, City Gas acquired a 16.9-mile high pressure 4-inch lateral from Florida Gas Transmission Company. The lateral stretches from the town of Perrine south to the city of Homestead. This purchase offered new and unserved territory to the Miami division operating territory, equaling approximately 100 square miles of newly franchised growth opportunity. Customers such as Parmen Kendall Foods, Miami Dade Water and Sewer, Miami Dade Community College, various new residential projects, and the US-1 commercial corridor from S.W. 200<sup>th</sup> Street to Florida City are now available for expanded commercial account growth.

In 2002, City Gas installed a new city gate station (Palm Bay Gate) to serve an area within its territory that had previously been unserved. This was accomplished in order to meet customer requests for natural gas that encompassed several new residential housing projects, a large commercial corridor, and the Brevard Community College campus (south). Additionally, this new expansion allowed a back feed and reinforcement of the northern portion of the existing distribution piping system.

In summary, the developments discussed as well as other changes in account activity and company planning indicate the need to revise currently prescribed depreciation rates.

The company has proposed October 1, 2003, as the implementation date for revised depreciation rates and recovery schedules. This 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.

Therefore, we find that this date is appropriate, and October 1, 2003, is approved as the implementation date.

III. CORRECTIVE RESERVE TRANSFERS

In considering the company's depreciation study, we review the reserve position for each account. In regards to reserve transfers, if significant surpluses and deficits exist, then it is appropriate to make corrective reserve transfers between accounts. The effect of prior depreciation rates, average service lives, and net salvage projections results in surpluses and deficits which should be addressed. We have determined that there are surpluses and deficits for the following accounts, and the company shall make the following corrective measures (transfers) to the reserve to correct existing reserve deficiencies in the accounts:

Account	Book Reserve	Transfers	Restated Reserve
	(\$)	(\$)	(\$)
380 - Services - Other than Plastic	12,099,061	58,336	12,157,397
387 - Other Equipment	167,166	(58,336)	108,830
390 - Structures & Improvements	598,920	182,217	781,137
391.3 - Computers	1,234,790	(162,964)	1,071,826
392 - Transportation Equipment	322,938	(73,676)	249,262
393 - Stores Equipment	17,198	(7,049)	10,149
394 - Tools, Shop, Garage Equip.	211,983	54,423	266,406
395 - Laboratory Equipment	11,733	7,049	18,782
Total	14,663,789	0	14,663,789

IV. DEPRECIATION RATES AND RECOVERY SCHEDULES

Our determinations of the remaining lives, net salvage values, reserve positions, and resultant depreciation rates and recovery schedules are shown on Attachment A. These changes are the result of a comprehensive review of City Gas's submitted data and

information by our staff. The investments and reserves reflect estimated amounts as of October 1, 2003, restated to reflect the transfers required above.

The company's original proposal reflected the currently prescribed average remaining lives with net salvage values based on 1999-2003 activity. Even with retaining the current underlying average service lives, average remaining lives warrant revision to recognize activity since the last review. Additionally, while recent activity can serve as an indicator of net salvage expectations, if retirement activity has been minimal, the indications cannot be considered reliable.

This filing was essentially a staff-assisted study. The company provided the necessary data for our staff to develop an average age for each account's surviving investment estimated as of October 1, 2003. Our staff and the company then worked together in developing appropriate life and salvage values.

As mentioned previously, since the company's 1999 study, Phase 1 of the East/West pipeline has been completed, approximately 50 miles, and has begun serving two customers, Florida Crystals and Wackenhut Prison. According to the company, contracts have been signed with three other parties and several more industrial projects are under development along the pipeline route. The company originally recorded the pipeline as transmission plant pursuant to the Department of Transportation's operating pressure designation for safety requirements and the transportation of gas. However, due to the current operating use and future plans to lower the existing pressure, City Gas believes the investment is more appropriately classified as distribution plant.

In 1996, the City Gas plant accounting department was transferred to New Jersey as part of NUI Utilities Inc.'s (NUI) decision to centralize plant accounting for all divisions. In 1998, NUI converted to a new fixed asset system. During the 1999-2000 period, City Gas discovered that its manual records did not match the data in its fixed asset system. Among other things, City Gas discovered that no detailed transactions for 1996-1997 had been loaded in the new system.

In resolving this problem and establishing continuing property records in compliance with regulatory requirements, City Gas management decided to move the plant accounting function back to Florida and reload all the capital asset data. The data used to reload City Gas assets were compiled from manual spreadsheets and original invoices maintained by the City Gas Plant Department. To streamline the process, surviving balances were loaded as a beginning point rather than all the historical annual additions, retirements, and transfer activity. All assets were input with their original acquisition date, accumulated depreciation and detailed descriptions, which included the type of asset, size of asset, quantity, FERC account code, and depreciation rate and life. Since the reload, City Gas continues to improve and automate the plant accounting process. The fixed asset system has undergone many customizations to improve the accuracy and reliability of the data.

As a result of the review and analytical process, City Gas has agreed with our staff concerning life and salvage values for each account. The changes in depreciation rates can be attributed to the following factors: updated ages to reflect activity since the last depreciation review, results of modifications and correcting the fixed asset system, and changes in the reserve position. The accounts with a substantial change in depreciation expense are outlined below.

#### A. Distribution Assets

##### Mains and Services (Accounts 376 and 380)

Mains and services comprise about 87-percent of the investment in the distribution plant function. The investment in the steel-mains account has experienced a 44-percent growth since the last study review; plastic mains has experienced a 41-percent growth. The growth in the steel-mains account is due to the East/West pipeline completed in 2001 and acquisition of the Homestead lateral in 1999. The plastic mains account growth reflects the significant expansion in Vero Beach, Port St. Lucie, and Brevard County.

For services, the investment in steel services has remained basically static since the last study. On the other hand, the investment in plastic services has experienced a 43-percent growth.

This reflects the fact that the majority of new service installations are plastic.

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.

The significant growth and additions to these accounts translate into a younger average age for the related investments, and a longer remaining life than last prescribed. The currently prescribed net salvage values remain reasonable and warrant no revision.

Measuring and Regulating Station Equipment (Account 379)

This account's investment reflects the addition of the new city gate station (Palm Bay Gate) in 2002 to meet customer growth. The 22-percent investment growth is reflected in the resulting average remaining life.

Meters and Regulators (Accounts 381 and 383)

Meters are used to measure gas consumption at the customer's premise, and regulators are used to regulate the gas pressure at the customer's premise. Pursuant to Rule 25-7.0461(6), F.A.C., the accounting treatment for meters and regulators 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.

Since the last depreciation review, the company has decided to discontinue refurbishing the majority of its residential and small commercial meters and regulators. City Gas found that the cost of refurbishment exceeds the replacement cost of a new meter or regulator, making refurbishment no longer cost-effective. Accordingly, when meters and regulators are retired, they are sold as scrap and replacement meters and regulators are purchased as needed.

In 2002, City Gas sold its meters and regulators to Fleet Bank as collateral to secure a low interest loan. The meters were then leased back to the company under an eleven-year capital lease agreement. Under the lease arrangement, City Gas is responsible for all testing and replacement. It is unclear what impact the capital lease agreement or the new policy regarding refurbishment will have on the lives and salvage values of these accounts. For this reason, maintaining the currently prescribed average service lives and net salvage values appears to be the more conservative action to take until the impact is more discernable.

Meter and Regulator Installations (Accounts 382 and 384)

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. According to the company, the costs of installation are not separated between the installation of the meter and the installation of the regulator. Based on analyzing the costs of a meter and regulator set, identifying the individual components, and then estimating the amount of labor required to install the components, City Gas allocates two-thirds of the total set installation cost to the meter and one-third of the cost to the regulator.

Meter and regulator installations are retired when the meter or regulator is removed from the location without a replacement, or when service through the meter or regulator is cut off. In other words, the life of these installations should be very similar to the life of services. Over the past couple of years City Gas has seen a high level of attrition in its residential and small commercial class. This increased customer turn-over has had an

impact on the meter and regulator installation accounts as seen by the increase in retirement activity.

The approved average remaining lives are the result of updating each account's age to reflect activity since the last represcription. The negative ten-percent net salvage value recognizes labor associated with the removal of these installations.

#### B. General Plant

During the course of our staff's review, it was discovered that adjustments were needed to the company's continuing property records for certain accounts. Specifically, some items of plant had been classified in the wrong account, thus requiring correction. The investment and reserve positions shown on Attachment B reflect these corrections.

##### Furniture (Account 391.1)

This account has experienced a fifteen-percent growth in investment since the company's 1999 depreciation review. This growth is due to the relocation of a customer service call center to Florida. The call center will handle calls for New Jersey and Florida. The relocation necessitated the purchase of additional furniture and communications equipment.

The company is in the process of completing a physical inventory for this account. As part of the inventory process, City Gas is bar coding the equipment to track on the continuing property record system.

##### Office Machines (Account 391.2)

In the process of reviewing the company's continuing property records, our staff determined that about 40-percent of this account's investment represented computer equipment. The investment and reserve positions shown on Attachment B reflect the corrective reclassifications. The recalculated average age of the surviving investment is 20.9 years, indicating a longer average service life than currently prescribed. Considering there are no near-term retirement plans, an average service life of 25 years



with a resulting 8.2 year average remaining life is approved. Recognizing the average age, it is not likely any salvage will be realized upon retirement. We find that a zero net salvage value is more in line with expected activity of this account than the currently prescribed 2-percent.

Computers (Account 391.3)

In 2001, the company entered into an operating lease agreement to upgrade its computers and software. As a result, all of the old equipment (\$1.2 million) was retired. The remaining investment is associated with servers and wiring. According to the company, the lease agreement will terminate in 2004, at which time City Gas will return to purchasing its computer equipment.

The average remaining life for computers recognizes the reclassification of investment from the office machines account.

Transportation Equipment (Account 392)

In 1996, the company entered into a capital lease agreement with Nations Bank for the purchase of all its vehicles. Currently, only 14-percent of the assets in this account are company owned. Maintenance expenses will drive the retirement of these vehicles.

Communications Equipment (Account 397)

This account has experienced a 46-percent growth in investment since the 1999 study. As part of the customer service call center relocation in 2001, NUI initiated a project to redesign its Interactive Voice Response (IVR) system by upgrading its software and hardware to current technology. As a part of the upgrade, the company designed new pathing and scripting specifications to support current and future customer service goals. The IVR, once upgraded, will also allow a "seasonal" increase in coverage and the company can prearrange staff for peak consideration. This change was implemented as a cost savings measure. It should result in more calls being completed within the IVR rather than the need for intervention of a more expensive customer service representative. The approved average remaining life reflects the growth in the account and recognizes that this equipment is subject to technological impacts.

V. INVESTMENT TAX CREDITS AND EXCESS DEFERRED INCOME TAXES

Earlier in this Order, we made revisions to the company's remaining lives, to be effective October 1, 2003. Revising a utility's book depreciation lives generally results in a change in its rate of Investment Tax Credits (ITC) amortization and flowback of excess deferred income taxes (EDIT) in order to comply with the normalization requirements of the Internal Revenue Code (IRC) and underlying Regulations (REGs) found in Sections 46, 167, and 168 and 1.46, 1.67, and 1.68, respectively.

Section 46(f)(6), IRC, states that the amortization of ITCs should be determined by the period of time actually used in computing depreciation expense for rate making purposes and on the regulated books of the utility. Since we have made a change in remaining lives, it is also important to change the amortization of ITCs to avoid violation of the provisions of sections 46 and 1.46, IRC and REGs, respectively.

Section 203(3) of the Tax Reform Act of 1986 (the Act) prohibits rapid flowback of depreciation related (protected) EDIT. Further, Rule 25-14.013, Accounting for Deferred Income Taxes Under SFAS 109, F.A.C., generally prohibits EDIT from being written off any faster than allowed under the Act. The Act, SFAS 109, and Rule 25-14.013, F.A.C., regulate the flowback of EDIT. Therefore, the flowback of EDIT shall be adjusted to comply with the Act, SFAS 109, and Rule 25-14.013, F.A.C.

Our staff, the Internal Revenue Service, and independent outside auditors look to a company's books and records and at the orders and rules of the jurisdictional regulatory authorities to determine if the books and records are maintained in the appropriate manner and to determine the intent of the regulatory bodies in regard to normalization. Therefore, the current amortization of ITCs and the flowback of EDIT should be revised to reflect the approved remaining lives. In order for there to be a clear audit trail, a prudent utility will revise ITCs and EDIT amortization and produce work papers to show how the revisions were made. The utility shall file detailed calculations of the revised ITC amortization and flowback of EDIT at the same time it files its surveillance report covering the period ending September 30, 2004.

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Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the corrective reserve transfers set forth in the body of this Order are approved and shall be made by City Gas Company of Florida. It is further

ORDERED that remaining lives, net salvages, and resulting depreciation rates set forth in Attachment A to this Order are approved, effective October 1, 2003. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, shall become final and effective upon the issuance of a Consummating Order unless an appropriate petition, in the form provided by Rule 28-106.201, Florida Administrative Code, is received by the Director, Division of the Commission Clerk and Administrative Services, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings" attached hereto. It is further

ORDERED that City Gas Company of Florida shall file detailed calculations of the revised Investment Tax Credit amortization and flowback of excess deferred income taxes at the same time it files its surveillance report covering the period ending September 30, 2004. It is further

ORDERED that 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 shall be closed upon the issuance of a consummating order.

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By ORDER of the Florida Public Service Commission this 14th  
Day of October, 2003.

BLANCA S. BAYÓ, Director  
Division of the Commission Clerk  
and Administrative Services

By: Kay Flynn  
Kay Flynn, Chief  
Bureau of Records and Hearing  
Services

( S E A L )

RRJ

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing that is available under Section 120.57, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing will be granted or result in the relief sought.

Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

The action proposed herein is preliminary in nature. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding,

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in the form provided by Rule 28-106.201, Florida Administrative Code. This petition must be received by the Director, Division of the Commission Clerk and Administrative Services, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on November 4, 2003.

In the absence of such a petition, this order shall become final and effective upon the issuance of a Consummating Order.

Any objection or protest filed in this/these docket(s) before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

ATTACHMENT A

ACCOUNT		COMMISSION APPROVED			
		AVERAGE REMAINING LIFE (YRS.)	NET SALVAGE RESERVE (\$)	10/1/03 ESTIMATED RESERVE (\$)	REMAINING LIFE RATE (\$)
<b>DISTRIBUTION ASSETS</b>					
375.0	Structures & Improvements	27.0	0.0	39.47	2.2
376.0	Mains - Other Than Plastic	26.0	(20.0)	47.22	2.8
376.0	Mains - Plastic	32.0	(20.0)	26.73	2.9
379.0	M&R Equipment - City Gate	26.0	(5.0)	28.99	2.9
380.0	Services - Other Than Plastic	11.8	(80.0)	95.72	7.1
380.0	Services - Plastic	27.0	(35.0)	31.10	3.8
381.0	Meters	14.5	0.0	38.82	4.2
382.0	Meter Installations	21.0	(10.0)	37.17	3.5
383.0	House Regulators	11.7	0.0	48.54 *	4.4
384.0	Regulator Installations	20.0	(10.0)	35.54	3.7
385.0	Industrial M&R Station Equipment	21.0	0.0	33.67	3.2
387.0	Other Equipment	10.4	0.0	69.84 *	2.9
<b>GENERAL PLANT</b>					
390.0	Structures & Improvements	27.0	0.0	32.50 *	2.5
391.1	Office Furniture	8.3	0.0	64.14	4.3
391.2	Office Machines & Equipment	8.2	0.0	84.25	1.9
391.3	Computers	2.6	0.0	56.58 *	16.7
392.0	Transportation Equip. - Combined	7.2	0.0	80.26 *	2.7
393.0	Stores Equipment	6.9	0.0	75.06 *	3.6
394.0	Tools, Shop, Garage Equipment	8.5	0.0	43.05 *	6.7
395.0	Laboratory Equipment	4.6	0.0	81.60 *	4.0
397.0	Communication Equipment	6.2	0.0	57.07	6.9
398.0	Misc. Equipment	11.3	0.0	24.59	6.7

\* Denotes restated reserve after corrective transfers.

CITY GAS COMPANY OF FLORIDA 2003 STUDY		
ACCOUNT	10/01/03 ESTIMATED INVESTMENT (\$)	10/01/03 ESTIMATED RESERVE (\$)
<b>DISTRIBUTION ASSETS</b>		
375 0 Structures & Improvements	556,250	219,530
376 0 Mains - Other Than Plastic	75,906,429	35,843,172
376 0 Mains - Plastic	42,967,953	11,486,316
379 0 M&R Equipment - City Gate	5,346,729	1,550,035
380 0 Services - Other Than Plastic	12,701,424	12,157,397
380 0 Services - Plastic	26,259,202	8,167,027
381 0 Meters	8,864,722	3,441,100
382 0 Meter Installatons	2,769,460	1,029,508
383 0 House Regulators	2,025,618	983,231
384 0 Regulator Installatons	1,212,061	430,741
385 0 Industrial M&R Station Equipment	2,731,334	919,623
387 0 Other Equipment	155,827	108,830
TOTAL DISTRIBUTION	181,497,009	76,336,510
<b>GENERAL PLANT</b>		
390 0 Structures & Improvements	2,403,498	781,137
391 1 Office Furniture	937,779	601,445
391 2 Office Machines & Equipment	503,923	424,541
391 3 Computers	1,894,355	1,071,826
392 0 Transportation Equip - Combined	310,571	249,262
393 0 Stores Equipment	13,522	10,149
394 0 Tools, Shop, Garage Equipment	618,829	266,406
395 0 Laboratory Equipment	23,017	18,782
397 0 Communication Equipment	1,325,266	756,316
398 0 Misc Equipment	240,670	59,177
TOTAL GENERAL PLANT	8,271,430	4,239,041
GRAND TOTAL	189,768,439	80,575,551

\* Denotes reserved reserve after corrective transfers