

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: January 16, 2008
TO: Office of Commission Clerk (Cole)
FROM: Division of Economic Regulation (Marsh)
Office of the General Counsel (Brown)
RE: Docket No. 070382-EI - 2007 depreciation study by Florida Public Utilities Company.
AGENDA: 01/29/08 - Regular Agenda - Proposed Agency Action - Interested Persons may Participate
COMMISSIONERS ASSIGNED: All Commissioners
PREHEARING OFFICER: Skop
CRITICAL DATES: None
SPECIAL INSTRUCTIONS: None
FILE NAME AND LOCATION: S:\PSC\ECR\WP\070382.RCM.DOC

Handwritten initials and signatures: JS, MCB, S.M.C., and a signature.

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COMMISSION CLERK

Case Background

Rule 25-6.0436(8)(a), Florida Administrative Code (F.A.C.), requires investor-owned electric companies to file a comprehensive depreciation study at least once every four years. On June 21, 2007, Florida Public Utilities Company (FPUC or company) filed its 2006 depreciation study in compliance with this rule. The company's last depreciation review was filed July 26, 2002, with an effective date of January 1, 2004. Staff has completed its review of FPUC's depreciation study and presents its recommendation herein.

The Commission has jurisdiction pursuant to Sections 350.115 and 366.05, Florida Statutes.

DOCUMENT NUMBER-DATE

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**Discussion of Issues**

**Issue 1:** Should the current depreciation rates for Florida Public Utilities Company be changed?

**Recommendation:** Yes. A review of the company's plans and activities indicates a need for a revision to the currently prescribed depreciation rates. (Marsh)

**Staff Analysis:** FPUC's last comprehensive depreciation study was filed on July 26, 2002. By Order No. PSC-03-1473-PAA-EI<sup>1</sup> the Commission approved revised depreciation rates and components, effective January 1, 2004. The company has filed this current study in accordance with Rule 25-6.0436, F.A.C., which requires electric companies to file a comprehensive depreciation study at least once every four years from the submission date of the previously filed study. A review of the company's activity data indicates the need to revise the depreciation rates.

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<sup>1</sup>Order No. PSC-03-1473-PAA-EI, issued December 31, 2003, in Docket No.020853-EI, In re: 2002 depreciation filing by Florida Public Utilities Company.

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**Issue 2:** What should be the implementation date for revised depreciation rates?

**Recommendation:** Staff recommends approval of the company's proposed January 1, 2008, date of implementation for revised depreciation rates. (Marsh)

**Staff Analysis:** Rule 25-6.0436(6)(b), F.A.C., requires that the data submitted in a depreciation study, including plant and reserve balances or company estimates, "shall be brought to the effective date of the proposed rates." The supporting data and calculations provided by FPUC match an implementation date of January 1, 2008.

**Issue 3:** What are the appropriate depreciation rates?

**Recommendation:** The recommended lives, net salvages, reserves, resultant depreciation rates, and recovery schedules are shown on Attachment A. Attachment B shows an increase in annual expenses of approximately \$125,247 based on January 1, 2008, investments. (Marsh)

**Staff Analysis:** Staff's recommendations are the result of a comprehensive review of FPUC's depreciation study. Attachment A shows a comparison of the currently approved depreciation rate parameters and those staff is recommending as appropriate, with which the company agrees. Attachment B shows a comparison of resulting expenses based on January 1, 2008, investments.

The company provided raw data as well as aging of the accounts. Additionally, the life and salvage values were developed jointly between staff and FPUC. As a result of the review and analytical process, staff and FPUC agree on lives, net salvages, and resulting depreciation rates for all accounts.

#### Depreciation Parameters

The recommended changes in the depreciation life characteristics and the salvage parameters for the distribution and general plant accounts can be attributed mainly to two factors: updated account ages to reflect activity since the last represervation, such as new investment; and changes in the associated reserve position. The accounts with substantial changes are discussed below.

In addition to its last depreciation study that was effective January 1, 2004, the company completed a rate case in 2004. Except as discussed below, changes are due to increased or decreased investment that results in a change in age. The current lives and rates are reasonable when compared with industry averages.

#### Account 350.1 – Land Rights

The company's filing showed an age of 43.5 years for this account. The previous study showed an age of 29 years. There has been no activity in the account, and there is no reason for the increase in the age. Staff has recalculated the age to be 33 years. A review of Schedule N of the company's filing shows that this is the correct age.

FPUC proposed an increase in the Average Service Life (ASL) from 50 to 56 years. This is in line with the industry average of 56.6 years. Therefore, staff believes the proposed increase should be accepted.

#### Account 352 – Structures and Improvements

The company proposes a change in ASL from 45 to 50 years. This is in line with the industry average of 49.4 years. Therefore, the change should be accepted. No other changes have been proposed, nor has staff identified any that are needed.

Account 353 – Station Equipment

The company proposes a change in ASL from 40 to 38 years. The industry average is 43.6 years. The change would move the ASL farther from the average. Staff's analysis shows that the current 40 year life is reasonable. Accordingly, staff believes the ASL should remain 40 years.

Account 354 – Towers and Fixtures

The current ASL of 50 years is in line with the industry average of 50.2 years. The company proposes a change in net salvage from -20 percent to -15 percent. Although this change moves away from the industry average, FPUC's own experience shows moderate amounts of salvage and cost of removal. The company's proposed change in salvage should be approved.

Account 355 – Poles and Fixtures

The company did not propose any changes to this account.

It has come to staff's attention that the company plans to replace the wood transmission poles with concrete poles as replacements are needed. Concrete poles have different life characteristics than wood poles. A review of industry averages shows that three other investor-owned electric companies in Florida have 40 to 50 year average service lives for transmission poles with -30 percent salvage. Staff believes it is appropriate to establish a sub-account, 355.1, for concrete transmission poles, with a 40 year ASL and -30 percent salvage.

Account 356 – Overhead Conductors and Devices

FPUC has proposed a change in net salvage from -20 percent to -10 percent, which reflects a reduction in cost of removal. Although this change diverges from the industry average, FPUC's own experience shows moderate amounts of salvage and cost of removal. The company's proposed change in salvage is appropriate.

Account 359 – Roads and Trails

This account shows an average age of 22.7 years. However, the average age of this account in the previous study was 41.1 years. An adjustment was made to the account in 1994. In subsequent studies, FPUC treated the entire account as having a 1962 vintage. Accordingly, staff has continued the age of 45.1 years, including the four years since the last study.

Account 361 – Structures and Improvements

FPUC proposes an increase in the ASL from 45 to 50 years. This is slightly higher than the industry average, but is within reason, since the company has vintages in the account dating back to 1959. No other changes are proposed.

Account 364 – Poles, Towers and Fixtures

The company proposes an increase in ASL from 33 years to 35 years, and a change in net salvage from -40 percent to -45 percent. Staff believes both of these changes are reasonable given the company's experience.

Account 365 – Overhead Conductors and Devices

FPUC proposes a change in net salvage from -30 percent to -35 percent, reflecting an increase in cost of removal. Staff believes this change is appropriate given the company's experience.

Account 369 – Overhead Services

FPUC proposes a change in net salvage from -30 percent to -35 percent, reflecting an increase in cost of removal. Staff believes this change is reasonable given the company's experience.

Account 370 – Meters

FPUC proposes a change in net salvage from -10 percent to -5 percent, reflecting an increase in cost of removal. This is in line with the company's recent experience and should be accepted.

Account 392.1 – Transportation – Cars

FPUC proposes a change in ASL from 6 to 8 years. Staff agrees with this proposal. The age of the cars in the account ranges from 5 to 8 years. Thus, a longer life is more representative of the actual experience. Staff notes, however, that the change causes volatility in the depreciation rate. Therefore, staff believes that it is appropriate to take a more gradual approach. Staff recommends a 7 year ASL.

Account 392.2– Transportation – Light Trucks and Vans

FPUC proposes a change in net salvage from 10 percent to 20 percent. This appears to be reasonable based on the company's experience. FPUC proposes a change in ASL from 8 to 10 years. However, as discussed above, staff believes a 9 year life would mitigate any resulting volatility in the depreciation rate.

Account 392.3 – Transportation – Heavy Trucks and Vans

FPUC proposes a change in ASL from 12 to 15 years. As discussed above, staff believes a 13 year life would mitigate any resulting volatility in the depreciation rate.

Account 392.4 – Transportation – Trailers

FPUC proposes a change in net salvage from 5 percent to 0. Although the company's experience has been limited, it shows a 10 percent salvage. The industry average is 28 percent. However, staff notes that this account has little activity. Therefore, staff believes it is appropriate to retain a 5 percent salvage at this time.

Account 396 – Power Operated Equipment

The company and staff agree that the ASL should be increased from 15 years to 20 years. No other changes are proposed. The industry average for this account is 13 years. However, FPUC stated that it has a policy of repairing equipment as necessary rather than replacing it, which the company believes has been the more cost effective approach. While there are pieces of equipment with vintages dating back to 1980, FPUC states that it has verified the existence of the equipment through a physical inventory. Therefore, staff believes a longer ASL is warranted.

**Issue 4:** Should the Commission make any corrective reserve allocations between accounts?

**Recommendation:** Yes. Staff recommends the reserve allocations as shown below. These allocations bring each account more in line with its theoretically correct reserve level. (Marsh)

**Staff Analysis:** As part of its review of the company's depreciation study, staff reviewed the reserve position for each account. When significant surpluses and deficits exist, corrective reserve transfers between accounts should be recovered as quickly as possible, unless such recovery prevents the company from earning a fair and reasonable return on its investments. The effect of prior depreciation rates, average service lives, and net salvage projections results in surpluses and deficits that should be addressed. The reserve transfers presented are based upon the company's planning and expectation of future retirements, which may further impact several plant account balances. As staff reviews the company's annual status report of plant accounts, it will continue to monitor the company's reserve position. For this reason, staff recommends transferring these related reserve surpluses to help correct the existing reserve deficiencies in the accounts as shown below.

RESERVE ALLOCATIONS					
Accounts		Projected 12/31/2007 Reserve	Theoretical Reserve	Recommended Allocations	Restated 01/01/2008 Reserve
<b>TRANSMISSION</b>					
350.1	Land Rights	\$35,031	\$33,120	(\$1,911)	\$33,120
352	Structures and Improvements	10,761	9,683	(1,078)	9,683
355	Poles and Fixtures - Wood	924,193	1,334,657	43,391	967,584
356	Overhead Conductors and Devices	633,447	593,045	(40,402)	593,045
<b>DISTRIBUTION</b>					
360.1	Land Rights	\$5,354	5,219	(\$135)	5,219
361	Structures and Improvements	32,732	28,813	(3,919)	28,813
366	Underground Conduit	598,956	512,012	(86,944)	512,012
367	Underground Conductors and devices	1,691,639	1,612,806	(78,833)	1,612,806
373	Street Lighting and Signal Systems	508,328	765,019	169,831	678,159
<b>GENERAL PLANT</b>					
390	Structures and Improvements	\$492,368	509,029	16,661	509,029
392.3	Transportation – Heavy Trucks	1,219,379	30,794	(7,746)	1,211,633
392.4	Transportation – Trailers	30,213	30,794	581	30,794
396	Power Operated Equipment	188,392	178,896	(9,496)	178,896
<b>Total</b>		<b>\$6,370,793</b>	<b>\$6,396,369</b>	<b>\$0</b>	<b>\$6,370,793</b>



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**Issue 5:** Should this docket be closed?

**Recommendation:** Yes. If no person whose substantial interests are affected by the Commission's 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. (Brown)

**Staff Analysis:** If no person whose substantial interests are affected files a timely request for a hearing within 21 days, no further action will be required and this docket should be closed upon the issuance of a consummating order.

FLORIDA PUBLIC UTILITIES  
 2006 DEPRECIATION STUDY  
 COMPARISON OF RATES AND COMPONENTS

ACCOUNT	CURRENT			STAFF RECOMMENDED			REMAINING LIFE RATE (%)
	AVERAGE REMAINING LIFE (YRS.)	NET SALVAGE (%)	REMAINING LIFE RATE (%)	AVERAGE REMAINING LIFE (YRS.)	NET SALVAGE (%)	ESTIMATED 1/1/08 RESERVE (%)	
<b>TRANSMISSION PLANT</b>							
350.1 - Land Rights	21.0	0.0	2.2	23.0	0.0	58.6	1.8
352 - Structures and Improvements	25.0	0.0	2.0	28.0	0.0	44	2.0
353 - Station Equipment	24.0	10.0	2.3	25.0	10.0	26.83	2.5
354 - Towers and Fixtures	24.0	(20.0)	2.2	16.5	(15.0)	76.73	2.3
355 - Poles and Fixtures- Wood	27.0	(30.0)	3.8	21.0	(30.0)	40.96	4.2
355.1 Poles and Fixtures - Concrete	N/A	N/A	N/A	40.0	(30.0)	0	3.3
356 - Overhead Conductors and Devices	31.0	(20.0)	3.2	28.0	(10.0)	31.6	2.8
359 - Roads and Trails	13.9	0.0	3.9	10.0	0.0	61.61	3.8
<b>DISTRIBUTION PLANT</b>							
360.1 - Land Rights	40.0	0.0	1.9	42.0	0.0	24.4	1.8
361 - Structures and Improvements	34.0	0.0	2.2	35.0	0.0	30	2.0
362 - Station Equipment	24.0	(10.0)	3.0	31.0	(10.0)	19.39	2.9
364 - Poles, Towers, and Fixtures	23.0	(40.0)	4.2	21.0	(45.0)	45.82	4.7
365 - Overhead Conductors & Devices	22.0	(30.0)	3.8	15.7	(35.0)	53.22	5.2
366 - Underground Conduit	41.0	0.0	2.0	41.0	0.0	18	2.0
367 - Underground Conductors & Devices	24.0	0.0	2.9	24.0	0.0	30.4	2.9
368 - Line Transformers	15.8	(20.0)	4.2	13.6	(20.0)	57.43	4.6
369 - Services	23.0	(30.0)	3.8	21.0	(35.0)	47.51	4.2
370 - Meters	15.4	(10.0)	3.6	14.3	(5.0)	51.69	3.7
371 - Installation on Customers' Premises	9.0	15.0	6.1	8.3	15.0	34.43	6.1
373 - Street Lighting & Signal Systems	14.6	(10.0)	5.6	9.5	(10.0)	55.4	5.7
<b>GENERAL PLANT</b>							
390 - Structures & Improvements	36.0	0.0	2.0	38.0	0.0	24.00	2.0
392.1 - Transportation-Cars	3.1	15.0	9.2	0.9	15.0	101.81	12.1
392.2 - Transportation-Light Trucks & Vans	3.9	10.0	11.3	3.1	12.0	72.70	4.9
392.3 - Transportation - Heavy Trucks	3.7	10.0	9.5	7.5	10.0	58.80	4.2
392.4 - Transportation - Trailers	20.0	5.0	4.0	17.7	5.0	27.74	3.8
396 - Power Operated Equipment	4.3	5.0	6.3	0.6	5.0	92.12	4.8

\*Denotes whole life rate.

**FLORIDA PUBLIC UTILITIES  
2006 DEPRECIATION STUDY  
COMPARISON OF EXPENSES**

ACCOUNT	01/01/2008 INVESTMENT	01/01/2008 RESERVE	CURRENT		STAFF RECOMMENDED		
			RATE	EXPENSES	RATE	EXPENSES	CHANGE EXPENSES
<b>TRANSMISSION PLANT</b>							
350.1 - Land Rights	56,519	33,120 *	2.2	1,243	1.8	1,017	(226)
352 - Structures and Improvements	22,006	9,683 *	2.0	440	2.0	440	0
353 - Station Equipment	2,426,032	650,825	2.3	55,799	2.5	60,651	4,852
354 - Towers and Fixtures	224,665	172,385	2.2	4,943	2.3	5,167	224
355 - Poles and Fixtures- Wood	2,362,224	967,584 *	3.8	89,765	4.2	99,213	9,448
355.1 Poles and Fixtures - Concrete	0	0	N/A	N/A	3.3 *	0	0
356 - Overhead Conductors and Devices	1,876,726	593,045 *	3.2	60,055	2.8	52,548	(7,507)
359 - Roads and Trails	6,788	4,182	3.9	265	3.8	258	(7)
<b>TOTAL TRANSMISSION PLANT</b>	<b>6,974,960</b>	<b>2,430,824</b>		<b>212,510.0</b>		<b>219,294.0</b>	<b>6,784</b>
<b>DISTRIBUTION PLANT</b>							
360.1 - Land Rights	21,388	5,219 *	1.9	406	1.8	385	(21)
361 - Structures and Improvements	96,042	28,813 *	2.2	2,113	2.0	1,921	(192)
362 - Station Equipment	6,829,966	1,324,529	3.0	204,899	2.9	198,069	(6,830)
364 - Poles, Towers, and Fixtures	9,406,626	4,310,305	4.2	395,078	4.7	442,111	47,033
365 - Overhead Conductors & Devices	9,969,920	5,306,467	3.8	378,857	5.2	518,436	139,579
366 - Underground Conduit	2,844,509	512,012 *	2.0	56,890	2.0	56,890	0
367 - Underground Conductors & Devices	5,305,283	1,612,806 *	2.9	153,853	2.9	153,853	0
368 - Line Transformers	13,697,939	7,866,743	4.2	575,313	4.6	630,105	54,792
369 - Services	8,546,991	4,061,074	3.8	324,786	4.2	358,974	34,188
370 - Meters	3,474,376	1,795,959	3.6	125,078	3.7	128,552	3,474
371 - Installation on Customers' Premises	2,183,360	751,668	6.1	133,185	6.1	133,185	0
373 - Street Lighting & Signal Systems	1,224,031	678,159 *	5.6	68,546	5.7	69,770	1,224
<b>TOTAL DISTRIBUTION PLANT</b>	<b>63,600,431</b>	<b>28,253,754</b>		<b>2,419,004</b>		<b>2,692,251</b>	<b>273,247</b>
<b>GENERAL PLANT</b>							
390 - Structures & Improvements	2,120,955	509,029 *	2.0	42,419	2.0	42,419	0
392.1 - Transportation-Cars	50,580	51,493 *	9.2	4,653	12.1	0	(4,653)
392.2 - Transportation-Light Trucks & Vans	569,013	413,693	11.3	64,298	4.9	27,882	(36,416)
392.3 - Transportation - Heavy Trucks	2,047,780	1,204,157 *	9.5	194,539	4.2	86,007	(108,532)
392.4 - Transportation - Trailers	111,010	30,794 *	4.0	4,440	3.8	4,218	(222)
396 - Power Operated Equipment	194,199	178,896 *	6.3	12,235	4.8	9,322	(2,913)
<b>TOTAL GENERAL PROPERTY</b>	<b>5,093,537</b>	<b>2,388,062</b>		<b>322,584</b>		<b>169,848</b>	<b>(152,736)</b>
<b>TOTAL RATES</b>	<b>75,668,928</b>	<b>33,072,640</b>		<b>2,741,588</b>		<b>2,862,099</b>	<b>127,295</b>

\*Denotes restated reserve after corrective transfers.

\*\*Denotes whole life rate