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# Public Service Commission

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TALLAHASSEE, FLORIDA 32399-0850

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

**DATE:** August 7, 2008

**TO:** Office of Commission Clerk (Cole)

**FROM:** Division of Economic Regulation (Slemkewicz, Bulecza-Banks, Kyle, Maurey)  
Office of the General Counsel (Hartman)

*Handwritten initials and signatures:* JS, JAK, ALM, [Signature], [Signature]

**RE:** Docket No. 080152-GU – Petition for approval of recognition of a regulatory asset under provisions of Statement of Financial Accounting Standard (SFAS) No. 71, by Florida City Gas.

**AGENDA:** 08/19/08 – Regular Agenda – Proposed Agency Action – Interested Persons May Participate

**COMMISSIONERS ASSIGNED:** All Commissioners

**PREHEARING OFFICER:** McMurrin

**CRITICAL DATES:** None

**SPECIAL INSTRUCTIONS:** None

**FILE NAME AND LOCATION:** S:\PSC\ECR\WP\080152.RCM.DOC

### Case Background

Florida City Gas (FCG or the Company) requests authority from the Commission to use deferral accounting and to create a regulatory asset to record certain charges incurred by the Company due to union decertification by FCG union employees. Specifically, these charges relate to the Company's requirement by federal law to fully fund FCG's estimated portion of the underfunded union pension liability. FCG is a division of Pivotal Utility Holdings, Inc. (PUHI), which became a wholly owned subsidiary of AGL Resources (AGLR) when AGLR merged with NUI Corporation on November 30, 2004. FCG is not requesting any rate adjustment at this time.

DOCUMENT NUMBER-DATE

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FPSC-COMMISSION CLERK

The Company's financial reporting is governed by Generally Accepted Accounting Principles, of which Financial Accounting Standards (FAS) are a part. Several of these standards pertain to employee benefits as detailed below:

- FAS 87 prescribes the accounting treatment of defined benefit pension plans.
- FAS 88 prescribes the accounting treatment of settlements, curtailments and terminations of pension plans.
- FAS 71 allows regulated companies to defer costs and create regulatory assets provided the regulatory agency grants authority for such a deferral. As stated in the introduction to FAS 71:

Regulators sometimes include costs in allowable costs in a period other than the period in which the costs would be charged to expense by an unregulated enterprise. That procedure can create assets (future cash inflows that will result from the rate-making process), reduce assets (reductions of future cash inflows that will result from the rate-making process), or create liabilities (future cash outflows that will result from the rate-making process) for the regulated enterprise. For general-purpose financial reporting, an incurred cost for which a regulator permits recovery in a future period is accounted for like an incurred cost that is reimbursable under a cost-reimbursement-type contract.

Additional qualification requirements under FAS 71 are stated in Section 9 of FAS 71:

Rate actions of a regulator can provide reasonable assurance of the existence of an asset. An enterprise shall capitalize all or part of an incurred cost that would otherwise be charged to expense if both of the following criteria are met:

- a) It is probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes.
- b) Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred costs rather than to provide for expected levels of similar future costs. If the revenue will be provided through an automatic rate-adjustment clause, this criterion requires that the regulator's intent clearly be to permit recovery of the previously incurred costs.

FCG is seeking the Commission's approval of deferral accounting and acknowledgement of the likelihood of recovery of the previously incurred pension and other postretirement benefit costs, in order to meet the requirements of FAS 71.

Docket No. 080152-GU  
Date: August 7, 2008

The Commission has jurisdiction pursuant to Sections 366.04, 366.06, and 366.07, Florida Statutes.

### Discussion of Issues

**Issue 1:** Should the Commission authorize Florida City Gas to use deferral accounting and to create a regulatory asset to record certain charges incurred by the Company due to union decertification by FCG union employees?

**Recommendation:** Yes. The Commission should authorize Florida City Gas to use deferral accounting and to create a regulatory asset to record certain charges incurred by the Company due to union decertification by FCG union employees. Further, the Commission should find that the approval to record the regulatory asset for accounting purposes does not limit the Commission's ability to review the amounts for reasonableness in future rate proceedings. (Kyle)

**Staff Analysis:** On February 15, 2008, FCG's unionized employees voted to decertify from the Teamsters' Union, and this vote was certified by the National Labor Relations Board on February 29, 2008. As a result of this decertification, the Company is under a legal obligation to pay its allocated portion of the underfunded pension liability ("liability") due to the withdrawal of union employees who had been covered under the union pension plan. The Company proposes to establish a regulatory asset to expense this liability over 15 years. Because the actual figures for the underfunded portion of the liability for a 2008 withdrawal are currently not available, the Company's analysis is based on the estimated liability it would have incurred if it had withdrawn from the Plan in 2007. FCG has claimed confidential treatment of the amount of the estimated liability because of its potential impact on ongoing settlement negotiations. The Company states that the actual number and corresponding liability should be available by late 2008, when the valuation of the Plan as of December 31, 2007, is complete.

Prior to the decertification, the Company contributed approximately \$80,000 annually to the Central States Pension Southeast and Southwest Areas Plan ("Plan"), a third-party, multiemployer plan which covered the unionized employees. This Plan is severely underfunded. FCG states that, historically, annual contributions to the Plan have been recovered through base rates as a component of the Company's cost of service. The Company has determined an estimated amount of the liability based on available, actual 2006 numbers, and states that this amount could be paid through one of two methods:

- A lump sum payment of the entire amount; or
- Annual payments for up to 20 years, including interest on the unpaid balance at a rate of 8% per year (based on the estimated annual rate of return of the pension plan).

FCG offers additional support for its request by providing a projection of increased annual pension costs that it would have incurred had the employees remained in the union. Further, the Company lists a number of operational and cost benefits which it believes will result from the elimination of restrictions on employee activities included in the previous union contract. Staff has analyzed these assertions and believes that FCG's analysis is reasonable.

FCG accounts for pension costs in accordance with FAS 87 and FAS 88. FAS 88 prescribes the accounting treatment of settlements, curtailments and terminations of pension plans. Staff believes that the situation described in FCG's petition is analogous to the handling of contractual termination benefits as described in Paragraph 15 of FAS 88, which states that:

An employer that provides contractual termination benefits shall recognize a liability and a loss when it is probable that employees will be entitled to benefits and the amount can be reasonably estimated. Termination benefits may take various forms including lump-sum payments, periodic future payments, or both. They may be paid directly from an employer's assets, an existing pension plan, a new employee benefit plan, or a combination of those means. The cost of termination benefits recognized as a liability and a loss shall include the amount of any lump-sum payments and the present value of any expected future payments.

FAS 71 allows regulated companies to defer costs and create regulatory assets, provided that it is probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes. To create a regulatory asset or liability, a regulated company must have the approval of its regulator. This concept of deferral accounting allows companies to defer costs due to events beyond their control and seek recovery through rates at a later time. The alternative would be for the Company to seek a rate case each time it experiences an exogenous event.

Staff believes FCG's request to create a regulatory asset to record charges incurred by the Company due to union decertification by FCG union employees meets the requirements of FAS 71 and should be approved. Further, staff believes that future recovery of costs resulting from curtailment, settlement or termination is implicit in a finding that FAS 71 is applicable. Finally, staff recommends that the Commission find that the approval to record the regulatory asset for accounting purposes does not limit the Commission's ability to review the amounts for reasonableness in future rate proceedings.

Docket No. 080152-GU

Date: August 7, 2008

**Issue 2:** Should this docket be closed?

**Recommendation:** Yes. 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. (Hartman)

**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.