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

**DATE:** April 9, 2009

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

**FROM:** Division of Economic Regulation (Gardner, Bulecza-Banks) *BB*  
Office of the General Counsel (Brown) *NCB JSB* *198*

**RE:** Docket No. 080170-GU – 2008 depreciation study by Indiantown Gas Company.

**AGENDA:** 04/21/09 – Regular Agenda –Proposed Agency Action - Interested Persons May Participate

**COMMISSIONERS ASSIGNED:** All Commissioners

**PREHEARING OFFICER:** McMurrian

**CRITICAL DATES:** None

**SPECIAL INSTRUCTIONS:** None

**FILE NAME AND LOCATION:** S:\PSC\ECR\WP\080170.RCM.DOC

### Case Background

Rule 25-7.045, Florida Administrative Code (F.A.C.), requires regulated natural gas companies to file a comprehensive depreciation study once every five years. On March 21, 2008, Indiantown Gas Company (Indiantown or company) filed its regular depreciation study in accordance with this rule. Indiantown's last comprehensive depreciation study was filed on January 14, 2003.

Staff has completed its review of the depreciation study and presents its recommendations herein. The Commission has jurisdiction to consider this matter pursuant to Sections 366.04, 366.05, and 366.06, Florida Statutes (F.S.).

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### **Discussion of Issues**

**Issue 1:** Should the currently prescribed depreciation rates of Indiantown Gas Company be changed?

**Recommendation:** Yes. A comprehensive review of Indiantown Gas Company's planning and activity since the prior depreciation filing indicates a need for a revision to the currently prescribed depreciation rates. (Gardner)

**Staff Analysis:** Indiantown's last comprehensive depreciation study was filed on January 14, 2003, with an effective date for revised depreciation rates of January 1, 2003. The current study is consistent with Rule 25-7.045, F.A.C., which requires gas utilities to file a comprehensive depreciation study at least once every five years from the submission date of the previously filed study.

During the 1993-2003 period, the company experienced significant commercial growth which was attributed to the addition of the US Generating Cogeneration facility. Currently, Indiantown is experiencing limited residential and commercial growth in its service environment due to the current downturn of the economy.

The Company officially separated its regulated and non-regulated activities by establishing Indiantown LP Gas Company, LLC (limited liability company). The Articles of Organization were filed with the Secretary of State, Division of Corporations, with an effective date of February 6, 2008. The company states that the change will enable them to streamline the accounting and finance functions, and to maximize two separate and different business models. The company sold fully depreciated plant equipment to the non-regulated side, and the proceeds or salvage received was applied to the corresponding plant account's depreciation reserves.

As discussed in subsequent issues, changes in activity and company planning since the last study indicates the need to revise currently prescribed depreciation rates.

**Issue 2:** What are the appropriate remaining lives, net salvage, reserve amounts, and resultant depreciation rates for Indiantown?

**Recommendation:** Staff's recommended remaining lives, net salvage values, reserves, and resultant depreciation rates are shown on Attachment A. The rates, based upon actual investments as of December 31, 2008, would result in a decrease in the annual depreciation expense of approximately \$5,125, as summarized on Attachment B. (Gardner)

**Staff Analysis:** Staff's recommendation is the result of a comprehensive review of the company's filed depreciation study. Attachment A shows a comparison of the current and proposed rate components (lives, salvages, and reserves) and the rate components staff is recommending for final approval. Investment and reserve positions, shown on Attachment B, reflect actual amounts as of December 31, 2008, with the reserve positions restated to reflect the staff's recommended corrective measures discussed in Issue 3.

A depreciation study provides an opportunity to review the present recovery position and determine whether any changes should be made to the existing pattern of recovery (depreciation rates). A prime concern of the depreciation study is life and salvage. As part of the review process, staff considers the prudence of company planning, including additions and retirements, technological impacts, retirement and salvage practices, and other related activities. The average service life refers to the overall period the account is expected to serve the public and is projected based on experience or estimates. The average remaining life is the remaining period of service which can be expected from the equipment or plant assets under study.

The company's filing provided aged retirement data for the 2004 through the 2008 period. The company provided the average age distributions of the surviving investments for each account. Staff worked with the company in the development of appropriate life parameters and salvage values. The review of each account's activity indicates that the service lives and curve shapes recommended in the last depreciation review remain reasonable. Staff and the company agree on lives, net salvages, and the resultant depreciation rates for all accounts as a result of the review and analytical process.

The recommended changes in depreciation rates can be attributed mainly to: 1) activity since the last depreciation study, 2) age recalculation by plant account, and 3) the correction of reserve positions by transfers to appropriate accounts. Staff will continue to monitor the reserve positions of the plant accounts when the company files its annual status report. A brief discussion of the plant accounts life parameters with a recommended change is set forth below.

#### Distribution Plant

##### Mains and Services

The company has completed several notable projects which increased its customer base and enabled it to comply with local and state requirements. These projects include: 1) a main replacement program which included replacing all ¾ inch steel mains with plastic mains, steel service lines, risers, meters, and regulators, 2) renovations to a six-inch gas main to comply with

the Department of Transportation requirements for a road construction project, and 3) updating the system pressure to accommodate the US Generating Cogeneration facility.

Mains and services comprise about 69 percent of the investment in the distribution plant function. In addition, mains and service lines are generally abandoned in place upon retirement. Activities involved in line abandonment are traveling to the site, 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 Indiantown, 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 in the same trench parallel to the existing pipe. The company's labor is not segregated between new installations and costs of abandoning the retired installation. The associated labor cost of abandoning the retired main or service is included with the capitalization cost of the new 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 the company's experience and expectations of the other Florida regulated gas companies.

#### Account 378-Measuring and Regulating Station Equipment-General

Currently, this account has an average service life of 35 years, a remaining life of 26 years, and a salvage factor of zero. The account includes regulators and other equipment used to maintain the correct operating pressure throughout the distribution system. At the time of the last study, two odorizers had been retired. The company required no additional assistance in the disposal of the first odorizer. The second odorizer was purchased in 1993 for \$3,306, and retired from service in 2001. This odorizer had 3-gallons of odorant remaining and required special disposal procedures based upon local and state laws. The company used Maverick Recovery Company to remove and dispose of 3-gallons of odorant from the premises at a cost of \$9,740. This removal cost is calculated to be approximately 20 percent of the \$47,982 investment into this plant account. Currently, the company is proposing a negative net salvage of 20 percent for this account, instead of the approved net salvage of zero percent. This change is to reflect the cost incurred to remove the odorant from the retired odorizer. Based upon the data presented, staff accepts the company's proposal as reasonable and recommends a negative net salvage of 20 percent on a going forward basis.

## General Plant

### Account 392-Transportation

This account consists of service trucks which are required in the operation of the distribution system. At the end of 2007, the company had a total of three service trucks. The current life parameters for this account are a 6-year service life and a 10 percent net salvage. During 2008, 2 fully depreciated service trucks were sold to the non-regulated entity. The salvage received was applied to the account's depreciation reserves. The company provided a detailed cost estimate of 2 new service trucks. The company is not requesting any change to the life parameters of this account. Based upon the data provided, staff recommends a 6-year service life and a 10 percent net salvage on a going forward basis.

### Account 394-Tools, Shop & Garage Equipment

This account consists of highly sensitive electronic leak detection equipment. Initially, the plant equipment in this account used a 20-year service life. The company states that the equipment represented a 10-year service life and proposes a change from a 20-year to a 10-year service life. Based upon the data provided, staff recommends a 10-year service life for this account on a going-forward basis.

### Account 397-Communication Equipment

The remaining plant investment for this account from the last depreciation study is the company's office telephone system. This account has an average service life of 15 years and a salvage factor of zero, but for this study, the company requested an 11-year service life. Thereafter, due to further company planning, the equipment was sold to Indiantown LP Gas, the non-regulated entity, at net value. The company states that the telephone service will be handled by Indiantown LP Gas. Currently, the companies are in two separate but connected buildings and any calls for Indiantown Gas will be transferred to the appropriate employee. Should the company add any new investment in this account, staff recommends a whole life depreciation rate based on an 11-year service life, S4 mortality dispersion, and a zero salvage factor, as indicated on Attachment A.

### Account 398 – Other Equipment

This account was established after the last depreciation study. It consists of a 2004 15KW Generac generator and a 2006 flatbed trailer. The generator is used to keep the utility building operations functioning during an emergency and the flatbed trailer holds the power generating equipment. Currently, this account is operating under a whole life rate of 10 percent. The company is proposing a 10-year service life and a salvage value of 5 percent. The average age of this plant account is 3.2 years. Based upon the analysis of the data provided by the company, staff accepts the company's request as reasonable and recommends a 10-year service life, and a 5 percent salvage value on a going-forward basis.

Account 399 – Computer Software

This is a new account established by the company in 2004 that consists of utility software for the customer database and financial applications. Also, in 2004, a major COBOL software update was required to keep the company's 12-year old customized utility package functioning. The company also purchased a new software package in December 2007 to meet its changing needs. The company maintains the old software since it contains necessary customer data. Also, the company has employed extra staff to convert the continuing property records to match the new software format. The company is proposing an 8-year service life and is operating under a whole life rate of 12.5 percent. Based upon the data presented and staff analysis, the age of the utility software is 2.9 years old with a remaining life of 5.1 years, a zero salvage value, and a resultant depreciation rate of 10.2 percent. Staff recommends the 8-year service life and zero net salvage for this account on a going forward basis.

**Issue 3:** Should the Commission make any corrections to the reserve allocations between accounts?

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

**Staff Analysis:** As part of its review of the company’s depreciation study, staff considered the reserve position for each account. When significant surpluses and deficits exist, corrective reserve transfers between accounts should be considered. The effect of prior depreciation rates, average service lives, and net salvage projections results in surpluses and deficits that should be addressed. For these reasons, staff recommends transferring these related reserve surpluses to help correct the existing reserve deficiencies in the accounts, as shown in the table below. The company should make corresponding entries to the related depreciation expense accounts.

RESERVES RE-ALLOCATION					
Account Number	Account Name	Actual Reserves (A)	Theoretical Reserves (B)	Reserve Transfers (C)	2009 Restated Reserves D=(A)+(C)
Distribution		(\$)	(\$)	(\$)	(\$)
376.0	Mains-Plastic	\$125,033	\$84,802	\$(33,994)	\$ 91,039
376.1	Mains-Steel	222,541	234,432	11,891	234,432
378.0	M & R Equipment	9,492	14,527	5,035	14,527
380.0	Services -Plastic	36,583	52,094	15,511	52,094
381.0	Meters	18,270	22,012	3,742	22,012
382.0	Meter Installations	3,269	2,785	(484)	2,785
383.0	House Regulators	4,968	5,389	421	5,389
385.0	M&R Equipment Industrial	63,905	61,783	(2,122)	61,783
	<b>Total</b>	<b>\$484,061</b>	<b>\$477,824</b>	<b>0</b>	<b>\$484,061</b>

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**Issue 4:** What should be the date of implementation for the new depreciation rates?

**Recommendation:** Staff recommends approval of the company's proposed January 1, 2009, date of implementation for the new depreciation rates. (Gardner)

**Staff Analysis:** Indiantown has proposed an implementation date for new depreciation rates of January 1, 2009. All data and related calculations that have been submitted support this date. Staff recommends approval of this date as being the earliest practicable date for utilizing the revised rates.



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**Issue 5:** 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. (Brown)

**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.

INDIANTOWN GAS COMPANY  
 2008 DEPRECIATION STUDY  
 RATE COMPONENTS

ATTACHMENT A

ACCOUNT	CURRENT			STAFF/COMPANY RECOMMENDED			
	AVERAGE REMAINING LIFE	NET SALVAGE	REMAINING LIFE RATE	AVERAGE REMAINING LIFE	NET SALVAGE	1/1/2009	REMAINING LIFE RATE
	(YRS.)	(%)	(%)	(YRS.)	(%)	(%)	(%)
<b>GAS DISTRIBUTION</b>							
376.1 Mains - Plastic	191,859	91,039 **	3.3	26.0	-30.0	47.45	3.2
376.2 Mains - Steel	249,316	234,432 **	4.2	10.9	-30.0	94.03	3.3
378.0 M&R Equipment - General	59,054	14,527 **	3.4	26.0	-20.0	24.60	3.7
380.0 Services - Plastic	105,882	52,094 **	3.3	22.0	-35.0	49.20	3.9
381.0 Meters	62,891	22,012 **	3.8	13.0	0.0	35.00	5.0
382.0 Meter Installations	15,471	2,785 **	2.6	29.0	-5.0	18.00	3.0
383.0 House Regulators	19,667	5,389 **	3.0	22.0	0.0	27.40	3.3
385.0 M&R Equipment - Industrial	99,570	61,783 **	3.5	11.5	0.0	62.05	3.3
387.0 Other Equipment	0	0	4.0	0.0	0.0	0.00	4.0
Total Distribution Plant	803,710	484,061					
<b>GENERAL PLANT</b>							
390.0 Structures & Improvements	171,895	43,740	2.5	32.0	0.0	25.45	2.3
391.0 Office Furniture	27,774	11,804	5.0	12.3	0.0	42.50	4.7
391.3 Computer Equipment	6,500	2,092	12.9	6.9	0.0	32.18	9.8
392.0 Transportation Equipment	106,661	43,176	14.8	4.3	10.0	40.48	11.5
394.0 Tools, Shop, and Garage Equip.	5,926	3,751	5.1	8.0	0.0	63.30	4.6
396.0 Power Operated Equipment	35,794	12,816	6.6	9.8	0.0	35.80	6.6
397.0 Communication Equipment	0	0	8.3	0.0	0.0	0.00	9.1 *
398.0 Misc. Equipment	13,647	4,722	NA	6.8	5.0	34.60	8.9
399.0 Computer Software	12,311	5,885	NA	5.1	0.0	47.80	10.2
Total General Plant	380,508	127,986					
Total Plant	1,184,218	612,047					

\* Denotes whole life rate.

\*\* Denotes restated reserve after corrective measures.

**INDIANTOWN GAS COMPANY  
 2008 Depreciation Study  
 COMPARISON OF EXPENSES**

Attachment B

ACCOUNT		INVESTMENT 1/1/2009	RESERVE 1/1/2009	CURRENT		STAFF/COMPANY RECOMMENDED		
				RATE	EXPENSES	RATE	EXPENSES	CHANGE IN EXPENSES
		(\$)	(\$)	(%)	(\$)	%	\$	\$
<b>GAS DISTRIBUTION</b>								
376.1	Mains -Plastic	191,859	91,039 **	3.3	6,331	3.2	6,139	-192
376.2	Mains -Steel	249,316	234,432 **	4.2	10,471	3.3	8,227	-2,244
378.0	M&R Equipment - General	59,054	14,527 **	3.4	2,008	3.7	2,185	177
380.0	Services - Plastic	105,882	52,094 **	3.3	3,494	3.9	4,129	635
381.0	Meters	62,891	22,012 **	3.8	2,390	5.0	3,145	755
382.0	Meter Installations	15,471	2,785 **	2.6	402	3.0	464	62
383.0	House Regulators	19,667	5,389 **	3	590	3.3	649	59
385.0	M&R Equipment - Industrial	99,570	61,783 **	3.5	3,485	3.3	3,286	-199
387.0	Other Equipment	0	0	4	0			
<b>Total Distribution</b>		<b>803,710</b>	<b>484,061</b>		<b>29,171</b>		<b>28,224</b>	<b>-947</b>
<b>GENERAL PLANT</b>								
390.0	Structures & Improvements	171,895	43,740	2.5	4,297	2.3	3,954	-343
391.1	Office Furniture	27,774	11,804	5 *	1,389	4.7	1,305	-84
391.3	Computer Equipment	6,500	2,092	12.9 *	839	9.8	637	-202
392.0	Transportation Equipment	106,661	43,176	14.8	15,786	11.5	12,266	-3,520
394.0	Tools, Shop, and Garage Equip.	5,926	3,751	5.1 *	302	4.6	273	-29
396.0	Power Operated Equipment	35,794	12,816	6.6	2,362	6.6	2,362	0
397.0	Communication Equipment	0	0	8.3	0 *	9.1	0	0
398.0	Other Equipment	13,647	4,722	0	0	8.9	1,215	1,215
399.0	Computer Software	12,311	5,885	0	0	10.2	1,256	1,256
<b>Total General Plant</b>		<b>380,508</b>	<b>127,986</b>		<b>24,975</b>		<b>20,797</b>	<b>-4,178</b>
<b>TOTAL PLANT</b>		<b>1,184,218</b>	<b>612,047</b>		<b>54,146</b>		<b>49,021</b>	<b>-5,125</b>

\* Denotes whole life rate.

\*\* Denotes restated reserve after corrective measures.