



Public Service Commission

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DATE: AUGUST 20, 1998

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BR/RO)

FROM: DIVISION OF AUDITING AND FINANCIAL ANALYSIS (SLEMKEWICZ, LEE)
 DIVISION OF ELECTRIC AND GAS (MILLS) *CM*
 DIVISION OF LEGAL SERVICES (C. KEATING) *wex RVE*

RE: DOCKET NO. 980723-GU - PETITION FOR APPROVAL OF ACCOUNTING METHODOLOGY FOR YEAR 2000 COSTS BY CITY GAS COMPANY OF FLORIDA.

AGENDA: 09/01/98 - REGULAR AGENDA - PROPOSED AGENCY ACTION - INTERESTED PERSONS MAY PARTICIPATE

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JDJ

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\AFA\WP\980723.RCM

CASE BACKGROUND

On June 9, 1998, City Gas Company of Florida (City Gas) filed a petition for approval to defer expenses incurred in the remediation of in-house data processing systems to Year 2000 compatibility and to amortize those expenses over a five year period. NUI Corporation (NUI), of which City Gas is an operating division, has undertaken a program of remediation, replacement and testing to address Year 2000 computer issues. The estimated cost to be incurred by NUI through September 30, 1998, is \$909,888 with \$200,175 being allocated to City Gas. The regulated portion of the \$200,175 that City Gas seeks deferral and amortization of is \$161,960.

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DIVISION OF RECORDS AND REPORTING

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission approve City Gas' petition to defer expenses incurred in the remediation of in-house data processing systems to Year 2000 compatibility and amortize those expenses over a five year period?

RECOMMENDATION: No. The Commission should deny City Gas' petition to defer and amortize expenses incurred in remediation of in-house data processing systems for Year 2000 compatibility. (SLEMKEWICZ)

STAFF ANALYSIS: As stated in the petition, NUI has incurred various capital expenditures and operating expenses in addressing Year 2000 compatibility issues. In some instances, programs and applications have been replaced and the costs capitalized. Computer hardware has also been assessed and any non-compliant hardware will be replaced and capitalized. The issue before the Commission is the accounting treatment of the expenses for the remediation of in-house developed systems that will not be replaced.

There is no question that City Gas must address the Year 2000 problem and Staff is not taking issue with City Gas' efforts to remediate any potential Year 2000 issues. However, Staff does not support City Gas' request to defer and amortize certain operating expenses that would normally be expensed as incurred. Expensing these costs as incurred is consistent with the accounting guidelines in EITF 96-14 concerning the expensing of costs associated with modifying internal software for the year 2000.

The Emerging Issues Task Force (EITF) was established by the Financial Accounting Standards Board (FASB) to assist the FASB in the early identification of emerging issues affecting financial reporting through the timely identification, discussion and resolution of financial issues within the framework of existing authoritative literature. The Task Force reached a consensus that external and internal costs specifically associated with modifying internal-use software for the year 2000 should be charged to expense as incurred. As a result, *EITF 96-14: Accounting for the Costs Associated with Modifying Computer Software for the Year 2000* was issued.

City Gas has asserted that these expenses are extraordinary and qualify for deferral and amortization. Staff would categorize these remediation expenses as out-of-the-ordinary, but not so

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extraordinary or having such a large financial impact that they could potentially distort City Gas' financial statements. The \$161,960 expense cited in the petition is less than 40 basis points on return on equity (ROE). Per City Gas' surveillance report for June 1998, its earned ROE is 6.71%, which is less than its authorized ROE midpoint of 11.30%. In addition, the deferral of these costs would create a regulatory asset that would remain on City Gas' books for five years.

It is Staff's opinion that City Gas has failed to sufficiently demonstrate the need to defer and amortize the expenses associated with the remediation of its in-house systems. Therefore, Staff recommends that City Gas' petition be denied and that City Gas expense these costs as incurred consistent with EITF 96-14. It should also be noted that these costs have not been reviewed for prudence or reasonableness and are, therefore, subject to review in future proceedings in which such costs are included.

Should the Commission approve City Gas' petition to defer and amortize these Year 2000 remediation expenses, Staff recommends that the approval be limited to the actual costs incurred as of September 30, 1998. City Gas should be directed to file a petition if it desires to defer and amortize any additional Year 2000 costs incurred after September 30, 1998.

ISSUE 2: Should this docket be closed?

RECOMMENDATION: This docket should be closed if no person, whose substantial interests are affected by the proposed action, files a protest within the 21 day protest period. (C. KEATING)

STAFF ANALYSIS: At the conclusion of the protest period, if no protest is file, this docket should be closed.