

FLORIDA PUBLIC SERVICE COMMISSION

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M E M O R A N D U M

September 26, 1996

TO : DIRECTOR OF RECORDS AND REPORTING (BAYO)

FROM : DIVISION OF AUDITING AND FINANCIAL ANALYSIS (HICKS) <sup>RM</sup>  
DIVISION OF ELECTRIC & GAS (MILLS) <sup>PSK</sup>  
DIVISION OF LEGAL SERVICES (JOHNSON) <sup>via RVE APC RT</sup>

RE : DOCKET NO. 960404-GU - PEOPLES GAS SYSTEM, INC., 1996  
DEPRECIATION STUDY

AGENDA: OCTOBER 8, 1996 - REGULAR AGENDA - PROPOSED AGENCY ACTION  
- INTERESTED PARTIES MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: S:\PSC\APA\WP\960404GU.RCM  
R:\960404GU.WX4

DISCUSSION OF ISSUES

ISSUE 1: Should currently prescribed depreciation rates be revised?

RECOMMENDATION: Yes. A review of Peoples Gas System, Inc.'s (Peoples or Company) plans and activity indicates a need for revision of current rates. (HICKS)

STAFF ANALYSIS: Under Rule 25-7.045(7), Florida Administrative Code, natural gas companies are to file a comprehensive depreciation study at least once every five years from the date of the last submitted study. The last depreciation study for Peoples was submitted March 8, 1991, with an implementation date of October 1, 1991. The Company filed the present study in keeping with this rule. The study represents an overall review of life and salvage parameters.

DOCUMENT NUMBER-DATE

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FPSC-RECORDS/REPORTING

**ISSUE 2:** What reserve transfers between accounts, if any, should be made?

**RECOMMENDATION:** Staff is not recommending any reserve transfers between accounts. Although a theoretical reserve analysis shows that the Airplanes account (Account 392.03) has an implied reserve surplus, staff recognizes that this account has a very short remaining life of 2.3 years. Rather than transferring the implied surplus now, staff recommends that the company book no further accruals in this account as it is fully accrued. Once retired and net salvage has been realized, any reserve imbalance can be addressed. (HICKS)

**STAFF ANALYSIS:** A theoretical reserve analysis indicates this account has an implied reserve surplus of approximately \$211,000. The remaining life of 2.3 years indicates the airplane is nearing the end of its life. Staff does not believe it is practical to transfer the implied reserve surplus when the airplane is nearing the end of its life and the company may or may not realize the salvage provided in the depreciation rate. It seems more appropriate to allow no further accruals in this account. If the company does not recover the full 25% salvage provided in the depreciation rate, it may petition the Commission for additional recovery.

Although the investment in this account is fully recovered, the single airplane is still in service. The company has plans to purchase a new aircraft, but it is not included in Peoples' budget for the upcoming fiscal year. If the current investment is still in service at the next represcription, and there are no plans to retire it, staff will consider a longer life.

Staff recommends no reserve transfers be made between accounts at this time. Staff does recommend, however, that no further accruals related to the embedded investment be allowed, and a whole life rate of 6.3% be provided for new airplanes placed in service during the next five years. The recommended net salvage related to any new aircraft is 25%.

ISSUE 3: What are the appropriate depreciation rates?

RECOMMENDATION: Attachment A reflects the depreciation rates recommended by staff, while Attachment B reflects the result depreciation expenses. Staff's recommendations, based on investments as of October 1, 1996, and reflected on Attachments A and B, would result in an increase in annual expenses of approximately \$140,000. (HICKS)

STAFF ANALYSIS: Staff's recommendations are the result of a comprehensive review of the Company's filed study. As a result of the review and analysis process, staff and the Company concur on lives, net salvages, and resultant depreciation rates for all accounts. Attachment A presents a comparison of the rate parameters (lives, salvages and reserves) proposed by the company and the rate parameters staff is recommending for approval. Attachment B, shows resulting expenses based on investments as of October 1, 1996. The recommended rates will result in an increase in annual expenses of approximately \$140,000. A brief discussion of salient matters is set forth below.

Distribution Plant

Structures and Improvements (Account 375)

The Company and the Staff agree on the remaining life and salvage parameters for this account. The remaining life is the result of using the service life underlying the currently prescribed remaining life and the current average age.

Mains and Services (Accounts 376 and 380)

Peoples is still in the process of completing a program of system upgrades to relieve water infiltration and to increase system pressures. The Company is replacing old cast iron pipe with plastic pipe to avoid further corrosion problems and to increase system pressure.

Surface restoration costs can be very high when a main or service is retired. 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.

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Staff believes that the company's proposed service lives and curve shapes for these accounts are reasonable and within industry estimates. They also reflect the experience of the activity in these accounts.

The Company's system upgrade program is reducing the instances of dissimilar metals and a smaller portion of the system will be under paving requiring costly surface restoration. As a result, the company believes that removal costs will be reduced because of an anticipated reduction in expensive surface restorations. Therefore, the recommended cost of removal factors for the Mains and Services Accounts are in line with the Company's estimates of labor time and material cost involved in abandonment under paving and not under paving for each category of Mains and Services.

Measuring and Regulating Station Equipment-General and City Gate (Accounts 378 and 379)

These accounts contain very similar types of equipment and therefore should be expected to have similar life and salvage characteristics. Account 378 consists of regulators and other equipment used to maintain the correct operating pressure throughout the distribution system. Account 379 is comprised of regulators and other equipment used to tie the distribution system to the transmission pipeline.

Staff finds no substantive reason to decrease the service life underlying the currently prescribed remaining life. The company proposes the use of an R1 curve shape to reflect the activity in these accounts. Therefore, the recommended remaining lives are based on an R1 curve shape, a 31-year service life, and the current average age for each account.

Peoples' proposed net salvage factor for each account of negative 4% is within the range of industry salvage estimates for this equipment. Staff recommends that the existing prescribed negative 4% net salvage should be maintained for each account.

Meters (Account 381)

The company proposed life and salvage factors for this account are reasonable and acceptable to staff.

Meter and Regulator Installations (Accounts 382 and 384)

Generally, installations are only retired either when the meter or regulator is removed from the location and no new one is installed, or when service through the meter or regulator is cut. In other words, the life of these installations should be very similar to the life of services. Peoples' last study reflected this position. However, the company now believes that its recently installed tracking system warrants a change in the general position regarding meter and regulator installations. For this reason, the company originally requested a shorter life for these accounts.

Peoples has recently developed enhanced software which allows the company to track meter and regulator installations on a detailed basis. With this software, a monthly report is generated which lists all meters that have been removed for inactivity, customer loss, etc. Since the vintage when the meter was originally installed on a specific premise is included on the report, meter and regulator installations of the same vintage are retired from the corresponding plant account. A new company policy requires these retirements on a monthly basis.

Rule 25-12.045, F.A.C.; Inactive Service Lines, requires the utility to take action regarding inactive service lines in two to five years if there is a prospect for reuse. As a result, the company has the option to wait two years before removing the meter if there is prospect for reuse. After five years of inactivity, the service line is physically retired. Under the circumstances, it seems that at most, the life of services would not exceed that of the installations by more than five years. Installations are rarely retired prior to the date the service ends or the meter is removed due to inactivity.

If there is no prospect for reuse, the rule requires that a service line be retired and physically abandoned within three months. However, the company states that its new policy is to retire the meter and regulator installations at the time the service ends, regardless of the prospect for reuse.

The company originally proposed an average service life of 20 years for meter and regulator installations. This proposal was considerably less than the service life of 28 years proposed for meters and the service life of approximately 33 years for services. Based on the company's proposal, the installations would be expected to retire prior to the meters.

Staff is recommending a 28 year average service life for these accounts because the average service life of the installation could conceivably be up to five years less than the life of the service,

but it should not be less than the service life of the meter. As a result, staff's recommended 28 year service life is the same as the company's proposed life of meters, but less than the weighted 33 year service life of services. Staff's recommendation considers some of the aspects of the company's new policy by reducing the current average service life of meter and regulator installations. However, the lack of documentation does not permit staff to reduce the average service life of these accounts beyond that of meters.

Therefore, the recommended remaining lives are based on an R3 curve shape, a 28-year service life and the current average age for each account. Staff also recommends a salvage factor of negative 18% for each account.

Regulators (Account 383)

Regulators are used to regulate the gas pressure at the customer's premise. As with meters, this investment is accounted for as cradle-to-grave. Staff finds that the 28 year service life proposed by the company is in line with industry estimates.

General Plant

Structures and Improvements (Account 390)

Staff understands that the Company leases its headquarters building. In the event the Company purchases a headquarters building before the next scheduled depreciation represetion, the investment should be assigned a 2.5% depreciation rate (40-year average service life with zero net salvage).

Office Furniture (Account 391)

An analysis of this account revealed that approximately 44% of the investment is related to modular furniture. Typically, modular furniture tends to have a shorter life expectancy than traditional wood furniture or its equivalent. As a result, staff believes the current 20 year average service life is no longer applicable. Staff's recommended average service life of 15 years represents a composite of an 18-20 year life for the wood furniture and a 10-12 year life for modular. Using a R1 curve shape and an age of 6.6 years, results in an average remaining life of 10.4 years.

Airplanes (Account 392.03)

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The Company has not retired the single aircraft in this account. Although Peoples does anticipate replacing the airplane in the near future, any purchase of a new aircraft will most likely occur after its fiscal year 1997. In any case, staff finds no compelling reason to change the current service life for this account.

Laboratory Equipment (Account 395)

An analysis of the account activity indicates an average service life of 18.5 years. Although the account activity is limited, there is no indication that the pattern of activity will change. This being the case, staff finds no compelling reason to maintain the current average service life of 25 years. Staff's recommended remaining life, at the current age, is based on a 20 year average service and life and a S1 curve. The net salvage of zero, as indicated in the study, is also recommended.

Communications Equipment (Account 397)

This account is comprised of mobile radios, base stations, cellular telephones, pagers, telephone systems and telemetering equipment. The study indicates an average service life of 9.7 years. As a result, staff finds no compelling reason to change the current service life for this account. A S3 curve shape, 10 year service life, and the current age underlie staff's recommended remaining life. In addition, staff recommends maintaining zero net salvage for this account.

ISSUE 4: What should be the implementation date for the new rates?

RECOMMENDATION: The Company has requested, and Staff recommends, implementation as of October 1, 1996. (HICKS)

STAFF ANALYSIS: Implementation as of October 1, 1996 will permit the recognition of more appropriate expenses for the fiscal year; also, the supportive data and calculations underlying the proposed new rates are based on this date. The Company has requested, and Staff recommends, implementation as of October 1, 1996.

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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, timely files a protest within 21 days, this docket should be closed. (HICKS)

STAFF ANALYSIS: Absent a protest of the Commission's proposed agency action, no further Commission action will be required. Therefore, this docket should be closed.