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(850) 413-6480

Public Service Commission

September 11, 1998

Mr. L. J. Defrain
Secretary/Treasurer.
South Florida Natural Gas
101 NW 202 Terrace
Miami, FL 33169

Re: Docket No. 980700 - GU

Dear Mr. Defrain:

Enclosed are two copies of the Staff Report of your current depreciation study filed in the subject docket. Please provide the Company Response by October 9, 1998 in order to meet our target date of December 1, 1998 for Agenda Conference. In your response, please provide us with any concurrences, differences, and/or additional input.

For your convenience we have enclosed a diskette containing the Staff Report formatted in WordPerfect, Version 6.1. If you have any questions concerning this review, please do not hesitate to contact Bob Holroyd at (850) 413-6471 or myself at (850) 413-6453.

Sincerely,

Patricia S. Lee
USC/Eng. Supervisor

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cc: Division of Records and Reporting
Division of Electric and Gas
Division of Legal Services
Office of Public Counsel

DOCUMENT NUMBER - DATE
10014 SEP 14 98
PSC-RECORDS/REPORTING

**STAFF REPORT
SOUTH FLORIDA NATURAL GAS
DOCKET NO. 980700-GU**

GENERAL

The company has proposed a July 1, 1998 date for implementation of new depreciation rates. This date coincides with the company's fiscal year. To accomplish this implementation date, an update of activity by account through June 30, 1998 was provided in response to staff's initial review. This update brings the investment and reserve accounts current to the date abutting the implementation of new depreciation rates. Where remaining lives are proposed in this report, they reflect staff recalculated average ages reflecting the updated activity. There are some questions regarding the updated activity which are discussed herein.

The company proposed remaining life for each account is the difference between the average service life and the average age. This implies all investment retiring simultaneously, with no ongoing retirements. Such a pattern of expected retirements (curve shape, retirement dispersion; or mortality dispersion) represents an idealized situation where the equipment is so designed and manufactured as to live efficiently until the precise year the company-determined replacing equipment was ready. In reality, there is no plant type where the company has such full control over retirement. The nearest would be heavy trucks or trailers, where maintenance problems and accidents can modify the pattern.

In selecting a curve shape, staff works from averages, modifying the average as necessary for any peculiarities of the given company. A basic premise is that a similar plant type, used in a similar fashion, will have the same curve shape.

Certain patterns of activity will change the curve shape. High retirements and/or high growth tend to increase early retirements (infant mortality). A stagnant situation has the opposite effect. Plant subject to theft, damage, or public requirements can be expected to have a greater incident of infant mortality than similar plant in a rural or small town setting.

The expected average service life for each account is estimated from an analysis of historic activity, expected impact of factors such as growth and technological change, and industry averages. Staff's review of each account's activity indicates that the service lives and curve shapes recommended in the last depreciation review basically remain reasonable.

DISTRIBUTION PLANT

1. **Structures and Improvements (Account 375):** This investment is comprised of fences and other protective improvements. Normally equipment such as this is expected to experience a life of about 25 years. However, recognizing an age of 23.8 years and the fact that there is no near-term plans for retirement of this equipment, staff proposes an average service life of 30

years with a SQ curve shape, resulting in an average remaining life of 6.2 years. Based on the nature of this investment, staff believes that the currently prescribed zero net salvage factor is appropriate.

2. **Mains (Other than Plastic) (Account 376)**: Staff proposes to maintain the current 38-year average service life and the R4 curve. By using the average age of 19 years, an average remaining life of 19.5 years results.

Staff proposes a net salvage factor of negative 45%. This recognizes the labor and material information supplied by the company in response to the initial review. It also reflects the fact that the majority of mains retired are not located under pavement.

3. **Mains (Plastic) (Account 376)**: There is limited data on this account to analyze. However, a review of the retirement rate does not indicate a change in curve shape or service life. Therefore, staff proposes a 38 year average service life, R4 curve shape, 4.9 year average age, and a resulting 33 year average remaining life.

When a replacement main is installed next to a main being retired, what removal costs are incurred by the retiring facility? Based on the labor and material information supplied by the company in response to the initial review, a net salvage of negative 15% is proposed.

4. **Measuring and Regulating Station Equipment - General (Account 378)**: This account has experienced no retirements since the last study review, but has grown more than 300%. In fact, most of the growth occurred in 1996. What was this growth associated with? Staff proposes maintaining the currently prescribed average service life of 34 years, R3 curve shape, and a negative 3% net salvage. Using an average age of 6.9 years produces an average remaining life of 27 years.

5. **Measuring and Regulating Station Equipment - City Gate (Account 379)**: In light of the lack of retirement experience, staff proposes the maintain the current 34-year average service life and R3 curve. An average age of 23 years results in an average remaining life of 13.6 years.

The currently prescribed negative 3% net salvage is in the range of reasonableness and is proposed by staff.

6. **Services - Other than Plastic (Account 380)**: The retirement rate for this account has averaged about 1.6% during the last five year period. The currently prescribed 36-year average service life and S2 curve shape are in the range of reasonableness. Use of an average age of 22.4 years results in an average remaining life of 16.1 years.

Service lines are cut at the edge of the pavement and abandoned in place. Based on the labor and material information supplied by the company in response to the initial review, staff proposes a net salvage factor of negative 60%. This recognizes the fact that the majority of steel services retired are not located under pavement.

7. **Services - Plastic (Account 480):** Retirements for this account have been insufficient to analyze for determination of life and salvage. This makes the reliance on industry averages necessary. Staff proposes maintaining the currently prescribed 36-year average service life and S2 curve. Using an average age of 5 years results in an average remaining life of 31 years.

Using the labor and material information supplied by the company in response to the initial review, staff proposes an negative net salvage of 40%.

8. **Meters (Account 381):** The activity of this account is consistent with the S4 curve shape. Further, an average service life of 29 years remains reasonable in light of the experience other companies have for this same type of equipment. An average age of 13.4 years results in an average remaining life of 15.6 years.

The current zero net salvage factor is in line with the account's activity and the range of reasonableness. Staff proposes maintaining this net salvage factor.

9. **Meter and Regulator Installations (Accounts 381,382):** When a meter or regulator is placed in a location which has never had a meter or regulator, or when an additional meter or regulator is added to an old locations (increasing the number at the location), the installation costs are capitalized. The installations are only retired when the meter or regulator is removed from the location and no new one is installed, or when the service through the meter or regulator is cut off. In other words, the life of the meter or regulator installation should be very similar to the life of services. Therefore, staff's proposal is based on the same average service life for the Services Account, Account 380. A 36 year average service life, S2 curve shape, 14.6 year average age, and 22 year average remaining life are proposed.

A negative 5% net salvage is proposed based on current industry expectations.

10. **House Regulators (Account 383):** The accounting treatment for this equipment is "cradle-to-grave." In other words, the cost of the regulator is capitalized immediately upon purchase and is not retired until junked. Costs for change-outs and refurbishments are expensed. Based on this and a review of the account activity, staff proposes an S4 curve, 30 year average service life, 9.2 year age, zero net salvage, and resulting 21 year average remaining life.

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11. **Industrial Measuring and Regulating Equipment (Account 385)**: The investment in this account is comprised of industrial measuring and station equipment located at the Boston Whaler plant in Edgewater. This equipment was placed in service in 1968 with no subsequent activity. From the company's response to the initial review, staff assumes there are no plans for retiring this equipment. Recognizing an average age of 29.5 years, staff proposes an average service life of 35 years, S4 curve, zero net salvage, and resulting 7.5 year remaining life.

12. **Other Equipment (Account 387)**: This account is comprised of distribution equipment not included in other accounts such as district pressure recorders, special pipe holders, and location signs. The investment has experienced a 42% growth rate since the last depreciation review with no retirement activity. Staff has recalculated the average age to be 6.9 years and proposes an S4 curve, 35 year average service life, zero net salvage, and resulting 28 year average remaining life.

GENERAL PLANT

13. **Structures and Improvements (Account 390)**: This account includes the improvements made at the leased office building for such things as mail holes, after hours payments equipment, fence, shell yard, air conditioner, and space heater. It also includes the construction of a warehouse. The January through June 30, 1998 activity submitted in response to the initial review indicates a retirement and reclassification taking place. According to the study, the retirement was for a fence and shell yard that was retired in April, 1998. However, the reclassification, according to the study, was recorded in April, 1998 from Account 394, Small Tools, to Account 391, Furniture Equipment, rather than to Account 390, Structures and Improvements. Please reconcile this discrepancy between the study and the activity so the average age can be recalculated and a remaining life determined.

14. **Office Equipment - Furniture (Account 391)**: According to the study, investment of \$2,565 associated with computer equipment should have been transferred from the furniture subaccount to the computer subaccount. However, according to the January through June, 30, 1998, activity submitted in response to the initial review, there is no indication of the computer subaccount or of the transfer mentioned in the study. Also, there is an addition of \$2,185 associated with a fax machine which staff believes should have been added to Account 491, Office Machines. Please reconcile this information so the average age can be recalculated and a remaining life determined.

15. **Computer Equipment (Account 391.1)**: The company proposed 5 year average service life, square wave curve, and zero net salvage is in the range of reasonableness for this equipment and is acceptable to staff. This investment was just added in 1997 making a whole life rate appropriate.

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16. **Office Machines (Account 491)**: This account has experienced only one retirement since the last study and that was the retirement of a Xerox machine in April, 1998. The remaining investment is fully accrued and no further accrual action should be taken. However, for any new machines added subsequent to January 1, 1998, staff proposes a 15 year service life, zero net salvage, and resulting 6.7% whole life rate.

17. **Transportation Equipment - Trucks (Account 392)**: According to the study and the company response to the initial review, \$3,166 related to truck repairs that the company has since reversed. However, there are also shown reclassifications of \$6,758 and \$7,491. Where were these reclassifications made to? The company stated in response to the initial review that the \$7,941 was sold in June 1998. If this is the case, why was it recorded as a reclassification/transfer? What vintage or vintages does the \$6,758 relate?

It is staff's understanding that the company records trade-in allowances as gains or losses. This activity should be properly treated as gross salvage and charged to the reserve. It is logical to assume some salvage will be realized upon the retirement of light trucks. For this reason, staff proposes 10% net salvage as being the minimum companies appear to realize.

18. **Small Tools (Account 394)**: In order to determine what impact, if any, the reclassification of the \$1,899 air conditioner has on the average age of this account, please provide the original placement year of this equipment.

19. **Laboratory Equipment (Account 395)**: The investment in this account is comprised of a 1982 vintage of odor level testing equipment. An average age of 15.5 years used with an S4, 20 year life table results in an average remaining life of 5.2 years.

When this equipment is retired, there will be little salvage, other than junk, realized. For this reason, a zero net salvage is proposed.

20. **Power Operated Equipment (Account 396)**: Staff is still unclear why the retiring dollars charged to plant in 1996 are different from those dollars retiring from the accumulated depreciation. Please explain specifically why the accumulated depreciation exceeded the cost of the engine by \$553. What does the \$553 represent?

The activity for January 1, 1998 through June 30, 1998 shows transfers/reclassifications/adjustments totaling \$22,447. Of this amount, \$1,722 appears to be associated with repairs to a pitching machine made at year-end 1978. Please explain the repairs capitalized in this instance as such activity is normally expensed. Additionally, this amount is quite similar to the amount retired to accumulated depreciation in 1996. It may be simply a coincidence but worth an inquiry.

Further, \$13,746 appears to be associated with a ditcher placed in 1985 and something else not identified in the amount of \$798 placed in service at year-end 1985. However, referring to the age distribution shown in the study, \$14,385 is shown surviving from the 1985 vintage with no surviving investment shown for the 1986 vintage. This means that more dollars are being transferred/reclassified out of the 1985 vintage than are surviving. At this point, please help us understand so the average age can be recalculated.

Additionally, where were the assets transferred/reclassified that are shown in the activity for the first six months of 1998.

21. **Communication Equipment (Account 397)**: We notice that the activity submitted in response to the initial review indicated an AT&T cellular phone in the amount of \$481 in service as of January 31, 1997. However, the age distribution shown in the study does not include this investment. To determine the impact this investment will have on the average age of this account, please provide the date this asset was placed in service. Once this information is received, a remaining life based on a 10 year life and an S3 curve shape will be calculated. These parameters are in line with industry estimates for similar plant.

Little salvage other than junk will be realized from the retirement of this equipment. A zero net salvage is therefore proposed.

22. **Miscellaneous Equipment (Account 398)**: This account has experienced insufficient activity for analysis for life and salvage. This makes reliance on industry estimates necessary. Using a recalculated age of 6.5 years and a 15 year average service life with an S4 curve shape, staff proposes an average remaining life of 8.5 years.

The company proposed zero net salvage is reasonable and acceptable to staff.