Response of the Attorney General to
Initial Data Request of Union Light Heat & Power Company to the Attorney General
Union Light Heat & Power Company
Case No. 2005-00042

Witness Responsible:
ROBERT J. HENKES

Question 29: Do you agree that certain performance objectives of ULH&P's AIP relate to matters which provide direct customer benefits, such as the reliability of ULH&P's service?

Response: Yes.

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Witness Responsible:
ROBERT J. HENKES

Question 30: If the answer to the preceding information request is in the affirmative, please state your opinion as to whether any portion of ULH&P's AIP expense attributable to performance objectives which relate to matters which provide direct customer benefits should be recovered through rates. Please respond as to your personal opinion, without regard to past Commission decisions.

Response: Mr. Henkes' personal opinion is that, at a minimum, all incentive compensation expenses that are dependent on corporate performance goals be made the full responsibility of the stockholder and be removed for ratemaking purposes. As stated on pages 38-39 of Mr. Henkes' direct testimony, this would include the disallowance in this case of all of the Company's LTIP expenses and almost 70% of the Company's AIP and UEIP expenses. However, as explained on pages 38-39 of his direct testimony, Mr. Henkes has reflected the removal of 100% of the Company's LTIP, AIP and UEIP expenses consistent with the Commission's ratemaking policy - established in ULH&P's prior Case No. 2001-092 - that the corporate performance goals in the Company's overall LTIP, AIP and UEIP plans in the current case continue to place more weight on the interests of ULH&P's stockholders than ratepayers.

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Witness Responsible:
ROBERT J. HENKES

Question 31: Regarding ULH&P's incentive compensation plans:

a. do you agree that, if the Company adds customers, this benefits the Company's shareholders by increasing net income, but also benefits existing customers by spreading fixed costs over a greater number of customers?

b. do you agree that, if the Company increases productivity, this benefits the Company's shareholders by increasing net income, but also benefits customers by keeping costs lower?

c. do you agree that, if the Company has higher net income, this could benefit customers by producing a better capital structure, and lowering financing costs?

Response: First, Mr. Henkes notes that to the extent that any of the above described scenarios indeed result in an increase in net income of the Company, all of the net income increases experienced in between rate cases will directly flow to the stockholders and will benefit the stockholders, not the existing customers.

a. Mr Henkes does not agree with the premise in this question that the addition of customers always causes an increase in a utility's net income. Added customers may result in an increase in fixed costs and the incremental revenues from added customers may not exceed the incremental costs.

b. Mr Henkes does not agree with the premise in this question that a productivity increase always causes an increase in a utility's net income. While a productivity increase may decrease a cost in one area, this cost decrease may only be realized by having an associated cost increases in another area.

c. Not necessarily.

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Witness Responsible:
ROBERT J. HENKES

Question 32: On pages 39 and 40 of Mr. Henkes' Direct Testimony, he recommends the removal of Governmental Affairs expenses for ratemaking purposes since "they have nothing to do with the provision of safe, adequate and reliable gas service."

a. state Mr. Henkes' understanding of the Company's activities involved with Governmental Affairs expenses.

b. if the Company classifies meetings with governmental officials to discuss matters relating to the Company's utility service (e.g., coordinating the local government's street improvements and the Company's main replacement so as to minimize the cost of street dig-ins and the number of times street traffic will be disrupted), would Mr. Henkes agree that such expense is a matter that involves the provision of safe, adequate and reliable gas service, and should be recovered through the Company's rates?

Response: The activities underlying the Governmental Affairs expenses of approximately $11,000 are described in the response to PSC-3-57 and were quoted on page 40 of Mr. Henkes' testimony.

It is Mr. Henkes' position that expenses for which the Company can prove, with convincingly reliable data, that they are required for the provision of safe, adequate and reliable gas service can be considered for ratemaking purposes and recovered in rates.

Mr. Henkes notes with regard to this issue that the Commission removed similar Governmental Affairs expenses in the Company prior gas base rate case, Case No. 2001-092. See Mr. Henkes' Schedule RJH-16, line 8 and footnote (8) in Case No. 2001-092, which expense adjustment was included in the Commission's total "miscellaneous" expense adjustment totaling $64,380 described on pages 34-36 of the Commission Order in that prior rate case.

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Witness Responsible:
ROBERT J. HENKES

Question 33: Refer to page 41, line 5, of Henkes Direct Testimony. Please reconcile the figure $22,299 amount for the slippage factor depreciation expense adjustment to the $17,205 indicated on page 20, line 2, and also to the figure shown on Schedule RJH-8, line 11. Please state which is the correct amount, which amount was actually used in calculating your recommended operating income, and the extent to which this results in any change to your recommended operating income.

Response: The $22,299 operating income adjustment referred to on page 41 of Mr. Henkes' testimony to reflect the after-tax impact of the slippage factor depreciation expense adjustment was later revised by Mr. Henkes to an income adjustment of $17,205, which is the correct amount, as shown on Schedule RJH-5, line 9. This "typo" was missed by Mr. Henkes during the final proofreading of his testimony.

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Witness Responsible:
ROBERT J. HENKES

Question 34: At page 44 of his Direct Testimony, Mr. Henkes states: "[t]here are no formal, written statements from the Kentucky Revenue Cabinet that would confirm that the Cabinet will no longer allow the Company to be assessed at below net book value."

a. is Mr. Henkes aware of any formal, written statements from the Kentucky Revenue Cabinet that would confirm that the Cabinet will continue to allow the Company to be assessed at below net book value through the end of the forecast test period?

b. if the answer to the preceding information request is in the affirmative, please provide references to all such formal, written statements.

Response: No.

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Witness Responsible:
ROBERT J. HENKES

Question 35: At page 45, lines 24-26 of his Direct Testimony, Mr. Henkes states that "the forecasted period 4% and 10% investment tax credit amortization of $69,130 was not, but should have been, included in the filing schedules for the forecasted period."

a. do you know whether the Company's effective tax rate calculation for this filing included the impact of the investment tax credit amortization?

b. assume that the Company's effective tax rate calculation for this filing included the impact of the investment tax credit amortization. If so, does this change your recommendation regarding investment tax credit amortization?

Response: Mr. Henkes is aware of the following with regard to the forecasted period 4% and 10% investment tax credit amortization of $69,130:

Based on Mr. Henkes' review of the Company's forecasted period income taxes claimed for ratemaking purposes in this case, Mr. Henkes has concluded that the Company's effective federal income tax rate used in the calculations is 35% and that no income tax credit for the forecasted period 4% and 10% investment tax credit amortization was reflected.

Schedule C-2, line 43 shows that $0 ITC amortization has been reflected in the determination of the forecasted period income taxes.

The response to AG-1-182 shows that, while the total 4% and 10% ITC amortization for the forecasted period is $69,130, ..."the Company's forecast did not include amortization of ITC. Since the Forecasted Period is based entirely on the forecast, the amount of ITC amortization is zero."

In its response to AG-2-11, the Company conceded that the amortization of ITC was not included in the income tax calculation for the Forecasted Period and that "The amortization of ITC was overlooked in this filing" and that "Yes, the annual ITC amortization should be included."

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Witness Responsible:
ROBERT J. HENKES

Question 36: Refer to page 46, line 21 through page 47, line 1 of Mr. Henkes' Direct Testimony. Please explain the basis for Mr. Henkes' understanding that it is Commission policy to use a five-year amortization period to flow back unprotected excess deferred income taxes. Provide the case number of any Commission decisions relied on by Mr. Henkes.

Response: The basis for Mr. Henkes' understanding is his review of Case No. 10064 in which the Commission ordered the 5-year amortization of unprotected excess deferred income taxes.

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Witness Responsible:
ROBERT J. HENKES

Question 37: Refer to Schedule RJH-5.

a. please show the calculation of the average forecasted period depreciable plant used in footnote 2.

b. please explain in detail why 100% of common land and land rights were excluded.

c. does Mr. Henkes agree that it would be correct to exclude only gas jurisdictional share of common land and land rights?

d. if the answer to the preceding information request is in the affirmative, please state how this affects your recommended operating income.

Response:

a. See Schedule B-3.2, pages 1-4:

Total Gas Plant Including Allocated Common:	$277,747,000
Less: Non-Depreciable Land and Land Rights:	
Account 304	(41,000)
Account 374	(36,000)
Company Account 1890	(1,190,000)
Total Depreciable Plant	$276,480,000

b. That was an inadvertent error. Only 38.13% of the common plant land and land rights of $1,190,000, or $453,747, should have been excluded.

c. Yes. See his response to part b.

d. The average forecasted period depreciable plant level (excluding land and land rights) should have been $277,216,253. Dividing Mr. Majoros' recommended forecasted period depreciation expenses of $6,827,000 into $277,216,253 results in a revised composite depreciation rate of 2.462%. Applying this revised composite depreciation rate to the AG's recommended $1,152,749 plant in service slippage factor adjustment results in a revised depreciation expense adjustment of $28,381 rather than the depreciation expense adjustment of $28,461 reflected on Schedule RJH-5. Thus, the entire difference to correct for the inadvertent error referenced in part b above is $80. On an after-tax basis, this difference is $48.

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Witness Responding: Michael J. Majoros, Jr.

38. At page 7, lines 12-15 of his Direct Testimony, Mr. Majoros states: "ELG [equal life group] ...results in...a higher depreciation rate than other alternative procedures which are typically used in Kentucky."

    a. describe the "alternative procedure(s) referred to in this statement;

    b. list the case number of each KyPSC decision using such "alternative procedure(s)"

    c. based on your review of KyPSC decisions relating to depreciation methodologies used by the KyPSC, did you become aware of any decisions (without regard to ULH&P's last gas rate case, which Mr. Majoros discusses in his testimony) where the KyPSC approved the use of an ELG methodology? If so, list the case number of each KyPSC decision.

Response:

See Mr. Majoros' response to Staff Data Request No. 1-12.

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Witness Responding: Michael J. Majoros, Jr.

39. Refer to page 19, lines 3-8 of Mr. Majoros' Direct Testimony and page 5 of Exhibit MJM-13. Provide a copy of any state utility commission decisions Mr. Majoros is aware of where the commission has expressly rejected the Traditional Inflated Future Cost Approach.

Response:

Please see the attached discussion of alternatives to TIFCA which have been accepted by state Commissions. Decisions are publicly available.

Alternatives to TIFCA Approved by Public Service Commissions

NARUC 1996 Public Utility Depreciation Practices Manual

> Some commissions have abandoned the above procedure [gross salvage and cost of removal reflected in depreciation rates] and moved to current-period accounting for gross salvage and/or cost of removal. In some jurisdictions gross salvage and cost of removal are accounted for as income and expense, respectively, when they are realized. Other jurisdictions consider only gross salvage in depreciation rates, with the cost of removal being expensed in the year incurred.[1]

New Jersey

Company: Rockland Electric Company
Docket No.: New Jersey BPU Docket Nos. ER02080614 and ER02100724
SK Witness: Michael J. Majoros, Jr.
Order(s): Initial Decision, June 20, 2003
Summary Order, July 31, 2003

Discussion of Results:

The New Jersey Board of Public Utilities Commission endorsed Mr. Majoros' testimony regarding SFAS No. 143, but used a net salvage allowance based on the average net salvage over a 10-year period, as recommended by Staff, instead of the five-year average recommended by Mr. Majoros.

As recommended by the Administrative Law Judge:

> RECO calculates its test year depreciation expense to be $5.194 million. RECO ib 128. RECO 30, Page 28-29. RECO 11A, Exhibit P-2, Page-11. The Ratepayer Advocate disputes the Company's figure and proposes a depreciation expense level of $3,864,000. Rib-74. Ratepayer Advocate witness Majoros also recommended that the amortization of the Theoretical Reserve Difference should be $1.103 million rather than the company's proposed amortization amount of $588,000. Ratepayer Advocate would exclude depreciation

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[1] National Association of Regulatory Utility Commissioners, Public Utility Depreciation Practices, August 1996 ("NARUC Manual"), page 157.

of the enhanced service reliability program and depreciation of post-test year plant. R-51. RJH-17.

Staff determined the depreciation expense to be $3,971,000. Sib Exhibit P-2, Schedule 13-14. Staff added a 10-year average net salvage of $150,000 to the total of $3,821,100. Sib 74.

The main controversy in the depreciation issue concerns net salvage and cost of removal and the interpretation of Statement of Financial Accounting Standards No. [143]. SFAS 143, paragraph B73. RECO rb Appendix 15.

Ratepayer Advocate witness Michael J. Majoros expressed his opinion that the company's depreciation proposal was unreasonable. In his pre-filed testimony Witness Majoros claims the Company's proposal will produce excessive depreciation and increase the revenue requirement. He also states the company's proposal is inconsistent with current thinking regarding cost, capital recovery and net salvage, particularly the cost of removal component of net salvage. R-36, Page 3. He traces the alleged excessive depreciation to a request for negative net salvage, which he claims, is unreasonable. R36-4. This results in an excessive revenue requirement. R-36-4. Witness Majoros recommends a depreciation expense of $3,863,900. R-36-20.

RECO witness Hutcheson disagrees with Mr. Majoros proposal and alleges that Majoros approach is a results driven exercise designed to under state depreciation rates, that he has pushed the recovery of net salvage far out into the future thereby relieving rate payers who benefit from the plant serving them today from any cost responsibility for retirement and removal of such plant. It imposes a cost on customers who never benefited from the plant to pay for its removal.

Staff concurs in part with the Ratepayer Advocate, supporting the intellectual foundation of FAS143, which supports "unbundled" depreciation rates, rates that exclude embedded cost of removal provisions. Staff would favor a cost of removal expense based upon a 10-year window of actual experience rather than the 5-year average used by the Ratepayer Advocate. Sib-74. Staff supports a $150,000

> annual negative net salvage provision. Staff recommends a test year depreciation expense of $3,971,000.
>
> I **FIND** that the Staff's test-year depreciation expense of $3,971,000 to be reasonable.[2]

The Board of Public Utilities further endorsed the position, modifying only the amortization period for the reserve excess:

> Based on our review of the extensive record in this consolidated proceeding, the Board has determined that the Initial Decision, subject to certain modifications, which will be set forth herein, represents an appropriate resolution of this proceeding. Accordingly, except as specifically noted below, and as will be further explained in a detailed Final Decision and Order which shall be issued, the Board HEREBY ADOPTS and incorporates by reference as if completely set forth herein, as a fair resolution of the issues in this consolidated proceeding, the Initial Decision.[3]
>
> All the parties in the base rate case agree that there is a significant excess depreciation reserve. The Company proposed a 20-year amortization of its calculated reserve excess of $11.8 million. The RPA claimed the proper reserve excess was $22.1 million, based upon the Company's asset lives, but excluding the Company's future net salvage assumptions from the depreciation rates. The RPA accepted the Company's proposal of a 20-year amortization. Both Staff and the ALJ adopted the RPA's recommendation. The Board HEREBY MODIFIES the Initial Decision so that the RPA's recommended level of excess reserve is amortized back to ratepayers over 10 years. The Board finds this to be an appropriate action in order to offset the increase associated with the deferred balances that were incurred over the 4-year transition period, as well as the increase in BGS charges for current service.[4]

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[2] I/M/O Rockland Electric Company, OAL Docket Nos. PUC 07892-02 and PUC 09366-02, BPU Docket Nos. ER02080614 and ER02100724, (Initial Decision, June 10, 2003), p. 47-49.

[3] I/M/O Rockland Electric Company, BPU Docket Nos. ER02080614 and ER02100724, Summary Order, July 31, 2003, p. 2.

[4] Id., page 3, item 3.

Alternatives to TIFCA Approved by Public Service Commissions

Company: Jersey Central Power & Light Company
Docket No.: New Jersey BPU Docket Nos. ER0208056, ER0208057, EO02070417 and ER02030173
SK Witness: Michael J. Majoros, Jr.
Order(s): Summary Order, August 1, 2003

Discussion of Results:

The Board agreed with Mr. Majoros that the inclusion of net salvage in depreciation rates was inappropriate. It adopted Mr. Majoros' recommendation of a $4.8 million net salvage allowance, based on the cost of removal included in JCP&L's test year budget for transmission, distribution and general plant.

As Ordered by the Board:

> Depreciation Expense. The Company is requesting a net depreciation expense annualization adjustment of $1,515,000 and total annualized depreciation expenses of $114,547,000. The Company maintains that it is complying with the terms of a June 27, 1996 stipulation ("Final Stipulation") approved by the Board, by updating the book depreciation rate computations annually for plant additions, retirement, transfers and adjustments and keeping the negative net salvage rate percentages and depreciation service lives consistent with the separate Stipulation of Settlement of Depreciation Rates, also dated June 27, 1996, which was also approved by the Board as part of the Final Stipulation. *I/M/O the Petitions of Jersey Central Power & Light Company for Approval of an Increase in its Levelized Energy Adjustment Charge, Demand Side Factor, Implementation of a Remediation Adjustment Clause (RAC) Other Tariff Changes, Recovery of Crown/Vista and Freehold Buyout Costs, Changes in Depreciation Rates, Settlement of Phase 1 of the Board's Generic Proceeding on the Recovery of NUG Capacity Payments,* Docket Nos. ER95120633, ER95120634, EM95110532, EX93060255 and EO95030398, (March 24, 1997). The Board HEREBY FINDS, consistent with the recommendations of the RPA and Staff, that the Company's inclusion of net negative salvage value in depreciation rates is inappropriate and instead, HEREBY ADOPTS utilization of a net salvage allowance of $4.8 million which is the cost of removal reflected in the Company's test-year budget for transmission, distribution and general plant. Accordingly, the Board

HEREBY ADOPTS a deprecation expense in the amount of $77,146,000.[5]

Company: Public Service Electric & Gas (Electric)
Docket No.: New Jersey BPU Docket No. ER02050303
SK Witness: Michael J. Majoros, Jr.
Order(s): Decision and Order, Issued April 22, 2004

Discussion of Results:

In the Company's 1997 Restructuring filing, the Company proposed extending the average life used to establish depreciation on the Company's distribution investment from 28 to 45 years, resulting in a 2.49% remaining life depreciation rate. That rate incorporated zero net salvage. The Company also proposed amortizing the resulting depreciation reserve excess over seven years. The Board agreed with the amortization of the reserve excess, however it adopted a three-year, seven-month amortization period. The Company began the amortization but continued to use the old 3.52% depreciation rate. The Company failed to change the rate to 2.49%.

In the 2003 case, Docket No. ER02050303, the Company did not submit a depreciation study. Instead, they proposed no changes to their existing distribution plant rates and changes to their general plant rates based on the rates resulting from a Settlement in their last gas base rate case.

Mr. Majoros recommended the use of the 2.49% depreciation rate consistent with the Company's proposal in the Restructuring filing. In addition, he calculated an additional reserve excess of $115 million resulting from the Company's continued use of the 3.52% depreciation rate and recommended that excess be amortized over the remaining period of the initial reserve excess amortization. Mr. Majoros recommended that the additional excess be amortized over 2 years of the remaining of the original amortization period.

The Board agreed that the 2.49% rate should have been in use beginning in August 1999. The Board accepted a Settlement proposed amortization period of 29 months for the reserve excess. At the present time, the Company is using a 2.49% remaining life depreciation rate (for Distribution). The rate incorporates zero percent net salvage.

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[5] I/M/O Jersey Central Power & Light Company, BPU Docket Nos. ER0208056, ER0208057, EO02070417 and ER02030173, Summary Order, August 1, 2003, p. 6.

Alternatives to TIFCA Approved by Public Service Commissions

Pennsylvania

The 5-year rolling net salvage allowance approach is used by the Pennsylvania Public Utility Commission in utility cases.[6] The allowance is incorporated as a separate specifically identifiable amount in depreciation expense. Depreciation rates do not incorporate future net salvage factors.

Vermont

Company: Central Vermont Public Service Corporation
Case No.: Vermont Docket Nos. 6946 and 6988
SK Witness: Michael J. Majoros, Jr.
Order(s): Order, Issued March 29, 2005

Discussion of Results:

Testifying for the Vermont Department of Public Service ("DPS"), Mr. Majoros recommended the use of a net salvage allowance based on a 5-year average of actual net salvage experience. As the Company had been experiencing positive net salvage on average, Mr. Majoros recommended $0 net salvage allowance. In addition, Mr. Majoros recommended that CVPS be required show collections for net salvage separately from accumulated depreciation through the use of subsidiary accounts.

While the Board did not implement Mr. Majoros' recommendation to use a $0 net salvage allowance, the Board did agree to the separate tracking of net salvage collections:

> The DPS has highlighted an important policy issue — in contrast to collections for depreciation, which enable the utility to recover costs that it has already incurred, collections for net salvage are, in essence, prepayments by ratepayers for expenses that the utility estimates it will incur at some point in the future. This is a significant distinction, and one that persuades us that collections for net salvage should be tracked and reported separately from other funds collected via depreciation expense. For this reason, we accept the DPS's recommendation that we require CVPS to follow the recording and reporting requirements of FERC Order 631 for Vermont jurisdictional ratemaking purposes. In other words,

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[6] See Penn Sheraton et. al. v. Pennsylvania Public Utility Commission, 198 Pa. Super. 618, 184 A. 2d. 234 (1962).

> CVPS must track and report its prior and future net salvage collections in a separate subsidiary account, and we expect this separate account to be shown in future cost-of-service filings.[7]

Missouri

Company: Laclede Gas Company
Case No.: Missouri GR-99-315
SK Witness: None
Order(s): Second Report and Order, Issued June 28, 2001

Discussion of Results:

In this case, the Commission Staff recommended that Laclede's future cost of removal be based on the actual cost of removal the Company was experiencing. The Commission agreed:

> Currently, Laclede is recovering more in depreciation for net salvage than it is spending. In addition, ratepayers will pay $2.3 million more in depreciation annually under Laclede's method of calculation. Under Laclede's theory, it would be allowed to recover from its *current* customers the estimated cost of *future* expenditures. Laclede has no definite plans for the removal of the major assets involved in this net salvage calculation. Laclede is not currently spending funds on the removal or salvage of these assets. Laclede's arguments for spreading the costs of the removal of these assets among different generations of customers were not persuasive because of the uncertainty of how much cost will be incurred for removal, when the removal will occur, or if the removal will occur at all. Therefore, the Commission finds that Laclede has failed to meet its burden of showing that its depreciation calculation for net salvage is just and reasonable. Laclede has not shown why it is just and reasonable to recover from its current customers more than its current expenditures for net salvage.

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[7] Investigation into the Existing Rates of Central Vermont Public Service Corporation, Docket Nos. 6946 and 6988, Order, Issued March 29, 2005, page 114.

> The Commission finds that Staff's proposed calculation of net salvage cost is just and reasonable. Staff's proposed calculation will allow Laclede to collect from its current customers the amount Laclede is currently expending for final net salvage cost for mass property accounts. Staff's calculation will also allow recovery of the amount Laclede is expending for interim cost of removal for life span property accounts. Thus, Staff's calculation will allow Laclede to recover the amounts it is currently spending for net salvage without overrecovering from its ratepayers, which is a just and reasonable result. This level of net salvage is adequate to allow Laclede to fully recover the net salvage of all plant.
>
> The Commission finds, therefore, that the calculation of net salvage cost in this case shall be performed in accordance with Staff's recommendations. Thus, current depreciation rates should reflect a net salvage component of the depreciation rate that, when multiplied by the plant balance, gives an annual accrual consistent with the current net salvage amounts experienced by Laclede. Laclede's current depreciation rates reflect this computation, and therefore, should remain unchanged, with the exception of Account 362, Gas Holders. This will result in an annual accrual of $21,054,647.[8]

Laclede appealed the Commission's decision to the Circuit Court of Cole County (Case No. 01CV325280) and then to the Missouri Western District Court of Appeals (Case No. WD61486). The appeal was dismissed and remanded to the Commission, with the instruction to provide clearer, more detailed findings of fact.[9]

The Commission reopened the case to take further evidence on the issues of depreciation and net salvage on May 4, 2004.[10] On January 11, 2005, Missouri's Public Service Commission reversed its position. However, it did require Laclede to separately track net salvage in the depreciation reserve.[11]

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[8] I/M/O Laclede Gas Company's Tariff to Revise Natural Gas Rate Schedules, Case No. GR-99-315, Second Report and Order, Issued June 28, 2001, pages 3-4.

[9] I/M/O Laclede Gas Company's Tariff to Revise Natural Gas Rate Schedules, Case No. GR-99-315, Order Directing Filing of Proposed Findings of Fact, Issued February 27, 2004, page 1.

[10] I/M/O Laclede Gas Company's Tariff to Revise Natural Gas Rate Schedules, Case No. GR-99-315, Order Setting Hearing and Prehearing Conference, Issued May 4, 2004, page 1.

[11] I/M/O Laclede Gas Company's Tariff to Revise Natural Gas Rate Schedules, Case No. GR-99-315, Third Report and Order, Issued January 11, 2005.

Alternatives to TIFCA Approved by Public Service Commissions

Company: Empire District Electric Company
Case No.: Missouri ER-2001-299
SK Witness: None
Order(s): Report and Order, Issued September 20, 2001.

Discussion of Results:

In this case, the Commission Staff again recommended that future net salvage be based on actual experience, and expensed, rather than be bundled into depreciation rates. The Commission agreed, stating:

> The Staff and Empire also disagree on whether depreciation rates should include net salvage value. Inclusion of net salvage value creates the need to project the date that plant will be removed, the cost of removal at the time it is removed and the gross salvage value, for plant that may never be removed or at least not be removed for some considerable time after it is retired. Unit 6 at Empire's Riverton site was retired, but presently remains on site. This uncertainty provides sufficient grounds to reject Empire's determination of net salvage cost. The Staff's approach of treating net salvage cost as an expense based on Empire's recent historical data reduces this uncertainty. Additionally, separately stating net salvage cost, rather than incorporating it in depreciation rates, appropriately identifies the significance of net salvage cost on rates. The Commission finds that net salvage cost considered in setting rates should be based on historical net salvage cost that Empire has actually incurred in the recent past and that it should be treated as an expense.[12]

The Commission Staff's treatment of net salvage remained unchanged in Empire's next rate case, Case No. ER-2002- 424. As stated in the Stipulation in that case, "consistent with existing Staff policy, the depreciation rates agreed to by the Parties do not include a provision for net salvage (cost of removal less salvage). Instead, net salvage has been included in the income statement in determining cost of service based upon the Company's actual historical experience."[13]

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[12] I/M/O Empire District Electric Company's Tariff Sheets etc., Case No ER-2001-299, Report and Order, Issued September 20, 2001, page 11.

[13] I/M/O Empire District Electric Company, etc., Case No. ER-2002-424, Report and Order, Issued November 14, 2002, Attachment A, page 4.

Alternatives to TIFCA Approved by Public Service Commissions

Company: Empire District Electric Company
Case No.: Missouri ER-2004-0570
SK Witness: Michael J. Majoros, Jr.
Order(s): Report and Order, Issued March 10, 2005

In Empire's most recent rate case, Case No. ER-2004-0570, Empire once again requested to incorporate net salvage as a component of depreciation rates. The Commission Staff recommended expensing net salvage, consistent with their existing policy, and Empire's existing rates. Mr. Majoros, testifying on behalf of the Office of Public Counsel, recommended a net salvage allowance based on the most recent five-years experience. On March 10, 2005, the Missouri PSC reversed it prior position.[14]

Oklahoma

Company: Empire District Electric Company
Cause No.: Oklahoma PUD 200300121
SK Witness: Mr. Majoros acted as consultant to the Commission, but not as witness.
Order(s): Order No. 478532, Issued July 31, 2003

Discussion of Results:

In this case Empire District Electric Company proposed the same depreciation rates that were ordered by the Missouri Public Service Commission in Case No. ER-2001-299. In other words, the depreciation rates proposed by the Company did not include a provision for net salvage. The Staff of the Oklahoma Corporation Commission agreed with the Company's proposal, specifically noting the net salvage issue.

> Staff's two major depreciation related issues are the salvage value and life assumptions made by the Missouri's Staff. Staff finds the salvage cost assumption as presented by the Missouri Commission acceptable. The first reason being that the Missouri Commission rejected Empire's proposed ratio of current net salvage (Gross Salvage less Cost of Removal) to the same Plant's original cost as a factor to multiply times current plant balance to estimate the net salvage that it anticipates will be required to remove the currently active plant from service decades in the future. Doing so would have helped Empire calculate a net salvage that is negative, nil, or positive meaning that the net

14 I/M/O Empire District Electric Company, etc., Case No. ER-2004-0570, Report and Order, Issued March 10, 2005.

> salvages [sic] becomes a cost. The net result in this case is a net salvage cost than [sic] can be as large or larger than the original cost of the same plant. Missouri proposed that the Company collect net salvage at the current level that the Company is experiencing. The Missouri Commission also determined that Empire would have collected $1.5 million more annually than it was spending for net plant removal (Net Salvage Cost).[15]

This case was settled in Order No. 478532, dated July 31, 2003. The Joint Stipulation and Settlement Agreement attached to that Order did not discuss depreciation.

Kentucky

Company: Jackson Energy Cooperative Corporation
Case No.: Kentucky 2000-00373
SK Witness: Michael J. Majoros, Jr.
Order(s): Order, Issued May 21, 2001

Discussion of Results:

Testifying for the Attorney General, Mr. Majoros recommended the use of a net salvage allowance based on a 5-year average of actual net salvage experience for distribution plant. The Commission agreed with his recommendation:

> The Commission agrees with the AG. ... Concerning the treatment of net salvage, while the Commission agrees that net salvage is normally recovered as part of the depreciation rates, the AG has offered persuasive reasons supporting a departure in this case from the normal approach. The Commission finds that it is reasonable under these circumstances to use the average net salvage allowance approach proposed by the AG. This approach should be utilized until Jackson Energy undertakes a new depreciation study.[16]

[15] I/M/O Empire District Electric Company, Cause No. PUD 200300121, Prefiled Responsive Testimony of Mutombo Lukasu, page 25.

[16] I/M/O The Application of Jackson Energy Cooperative for an Adjustment of Rates, Case No. 2000-373, Order Issued May 21, 2001, pages 33-34.

Company: Fleming-Mason Energy Cooperative Corporation
Case No.: Kentucky 2001-00244
SK Witness: Michael J. Majoros, Jr.
Order(s): Order, Issued August 7, 2002

Discussion of Results:

Mr. Majoros testified on behalf of the Attorney General in this proceeding. As in the Jackson Energy case, he recommended the use of a net salvage allowance:

> The AG proposes that the net salvage component normally included in depreciation rates be recovered using an average net salvage allowance approach, which is similar to the approach adopted for Jackson Energy. Under the AG's proposal, an amount representing the 5-year average net salvage experience is added to the distribution plant remaining life depreciation expense in lieu of Fleming-Mason's proposed net salvage ratios. The amount should be prorated to the accounts in proportion to actual net salvage experience. The AG recommends this approach for at least the next 5 years, at which time another depreciation study could be conducted.[17]
>
> Fleming-Mason has not offered comments on nor expressed concerns about the AG's proposal.[18]
>
> The Commission agrees with the AG. While the Commission agrees that net salvage is normally recovered as part of the depreciation rates, the arguments offered by the AG are persuasive reasons for supporting a departure in this case from the normal approach. The Commission finds that it is reasonable under the circumstances in this case to use the average net salvage allowance approach proposed by the AG. This approach should be utilized until Fleming-Mason undertakes a new depreciation study.[19]

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[17] I/M/O Adjustment of Rates of Fleming-Mason Cooperative, Case No. 2001-00244, Order Issued August 7, 2002, pages 22-23.
[18] Id., page 23.
[19] Id.

Alternatives to TIFCA Approved by Public Service Commissions

Michigan

Company: Consumers Energy Company
Case No.: Michigan U-12999
SK Witness: Charles W. King
Order(s): Proposal For Decision, Issued June 28, 2004
Opinion and Order, Issued October 14, 2004
Order Initiating Generic Proceeding, Issued October 14, 2004

Discussion of Results:

In this case, Snavely King testified on behalf of the Attorney General. Mr. King recommended "basing net salvage factors on the ratios of the most recent five years of actual salvage experience to plant-in-service."[20] The ALJ recommended that the Commission adopt the net salvage ratios and recommended removal cost allowances set forth by Mr. King.

The Commission recognized that net salvage was a major issue it its Opinion and Order:

> Consumers would continue the traditional approach to calculating and recovering net salvage; that approach maintains the *status quo* but does not address the singular issue raised by the remaining parties regarding the absolute size of the negative net salvage values proposed by Consumers and the formidable present net-salvage level within the company's books. The Staff's position reduces net-salvage values through the use of a five-year rather than a ten-year average of recent experience, but (as pointed out by Consumers) does so through use of a simplified company-wide average rather than on a functional plant group basis. Such an approach can mask anomalies that may exist within specific classes of gas utility plant. ABATE advocates utilization of a completely revised approach—net-salvage cost would become an expense item separate from depreciation and collected as such in Consumers' rates. The Attorney General would also separate net salvage from depreciation, but would recover that cost through depreciation expense, albeit with a similar current-cost result

[20] I/M/O Consumers Energy Company, Case No. U-12999, Proposal For Decision, Issued June 28, 2004, page 15.

> as ABATE. This "separation" concept has not been adopted in Michigan before, although other state commissions have considered it.[21]

However, the Commission was concerned with the magnitude of the net salvage adjustments proposed by the parties, including the AG.

> The gulf between the positions of the various parties is approximately $50 million in the amount of annual depreciation expense that is appropriate for recovery, or approximately one-half of the amount that the Commission has previously found appropriate as a depreciation expense for Consumers. The effect of such a considerable shift in cost recovery on both customer rates and quality of service could similarly be large, and it should not be undertaken lightly. The Commission is persuaded that the abrupt shift in the method and the manner of cost of removal recovery as proposed either by ABATE or the Attorney General is ill-advised at this juncture without further industry-wide comment, discussion, and review. The Commission provides for this in a companion order issued today in Case No. U-14292.[22]
>
> The Commission is equally not persuaded that a shift to a simplified five-year company-wide average as proposed by the Staff should be implemented. However, the Commission is concerned that the large negative net-salvage values that result from Consumers' analysis of ten years of data (or the projected costs for storage wells and related matters) do not provide an accurate illustration of the costs that Consumers will bear to retire its assets in the future. The large variance between Consumers' incurred removal costs and its projected costs has been amply pointed out by the Attorney General and by ABATE. Thus, Consumers' proffered rates will not alleviate this concern of the remaining parties.[23]

The Commission decided that the Company should continue to use its existing depreciation rates for the time being. In addition, the Commission opened a Generic Proceeding to "review Statement of Financial Accounting Standards No. 143, Federal

[21] I/M/O Consumers Energy Company, Case No. U-12999, Opinion and Order, Issued October 14, 2004, pages 12-13 (emphasis added).
[22] Id., page 13.
[23] Id.

Regulatory Commission Order No. 631, and their accounting and ratemaking issues (as well as other matters that are related to the retirement of tangible long-lived assets and the associated asset retirement costs) for Commission-jurisdictional electric and gas entities."[24] As of January 2005 this generic proceeding was just getting underway.

Georgia

Company: Georgia Power Company
Docket No.: Georgia 4007-U
SK Witness: Charles W. King
Order(s): Order, Issued 1991

Discussion of Results:

As described in the Georgia Public Service Commission's April 29, 2002 Proposed Final Order, Atlanta Gas Light Docket No. 14311-U, "In 1991, in Docket No. 4007-U, and again on December 20, 2001 in Docket No. 14000-U, the Commission approved a procedure [recommended by Staff witness Charles W. King] for computing net removal and salvage ratios for the Georgia Power Company that avoids the distorting effect of comparing dollars of very different values. Under this procedure, the utility develops an estimate of the total current cost of removing all existing plant in each account. This estimate is then ratioed to the current investment in the existing plant to derive the net removal cost ratio."[25]

Company: Georgia Power Company
Docket No.: Georgia 14000-U
SK Witness: Charles W. King
Order(s): Order, Issued December 20, 2001

Discussion of Results:

As explained above, the Georgia Public Service Commission first adopted Mr. King's recommended depreciation rates for this Company in 1991, Docket No. 4007-U. Mr.

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[24] I/M/O Commission's Motion to Establish Appropriate Accounting and Ratemaking Treatment for Statement of Financial Accounting Standards No. 143, Case No. U-14292, Order Initiating Generic Proceeding and Notice of Hearing, Issued October 14, 2004, page 6.

[25] IN RE: Earnings Review to Establish Just and Reasonable Rates for Atlanta Gas Light Company, Georgia Public service Commission, Docket No. 14311-U, Proposed Final Order of the Public Service Commission's Advocate Staff

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King's rates included a provision for net salvage which was calculated by developing an estimate of the total current cost of removing all existing plant in each account and then applying that estimate to the current investment in the existing plant to derive the net removal cost ratio. This methodology is different from the "traditional" methodology used by GA Power and other companies in that it removes the distortion caused by comparing current cost of removal dollars to very old retirement dollars.

In the Company's 2001 rate case, Georgia Power Company filed depreciation rates using that procedure and the Commission again agreed with Mr. King's recommended rates, which included the same net salvage methodology in use since 1991. In this case, the Commission adopted an Alternative Rate Plan, which included the following language:

> The Company shall reduce its annual depreciation expenses by $66.548 million to reflect the depreciation rates recommended by Staff, except that the Company shall utilize a fifty-year life for setting depreciation rates for Plant Vogtle.[26]

Company: Georgia Power Company
Docket No.: Georgia 18300-U
SK Witness: Charles W. King
Order(s): Order, Issued December 22, 2004.

As in the previous GA Power Rate cases, Mr. King testified on behalf of the Georgia Public Service Commission's Adversary Staff. Georgia Power once again, used Mr. King's recommended net salvage approach. However, in the 2004 rate case, he also recommended "the complete separation of pure depreciation, that is, the recovery of capital investment, from the recovery of net removal costs."[27] Mr. King proposed "separate schedules of rates for these two functions", using his net salvage recommendations.[28]

Although it is not explicitly stated in the Order, it is Mr. King's understanding that with the exception of the life span for Plant Vogtle, the Commission adopted his depreciation rate recommendations, including those for net salvage.

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[26] Georgia Power Company's 2001 Rate Case, Docket No. 14000-U, Order, Issued December 20, 2001, Exhibit A, Consent to Alternative Rate Plan.

[27] Georgia Power Company's 2004 Rate Case, Docket No. 18300-U, Direct Testimony of Charles W. King, page 4.

[28] Id.

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Company: Atlanta Gas Light Company
Docket No.: Georgia 14311-U
SK Witness: Charles W. King
Order(s): Order, Issued April 29, 2002

Discussion of Results:

In this case, Mr. King recommended the same net salvage methodology for Atlanta Gas Light that had been ordered for, and in use by Georgia Power Company since 1991. The procedure calls for the utility to develop an estimate of the total current cost of removing all existing plant in each account and then ratio that estimate to the current investment in the existing plant to derive the net removal cost ratio. This methodology removes the distorting effect of comparing dollars of very different values from the net salvage ratio.

The Commission agreed with Mr. King's recommendations:

> The Commission further finds that it is reasonable to require the Company to utilize the depreciation rates recommended by the Advocacy Staff witness Mr. King.[29]

Company: Atlanta Gas Light Company
Docket No.: Georgia 18638-U
SK Witness: Charles W. King
Order(s): Order, Issued April 27, 2005

In this case, Mr. King, testifying on behalf of the GPSC Adversary Staff, recommended the use of "two sets of rates, one being "pure" depreciation rates that only recover capital previously expended, and the other removal cost rates that accrue funds to remove, dismantle or otherwise dispose of property currently in service."[30] Additionally, Mr. King recommended "the Commission retain the present system for developing removal cost allowances. That procedure compares an estimate of the lifetime cost of removal, expressed in current dollars, to the original cost of each account that may incur such costs."[31]

The Commission agreed, stating:

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[29] I/M/O Atlanta Gas Light Company, Docket No. 14311-U, Order, Issued April 29, 2002, page 6.
[30] I/M/O Atlanta Gas Light Company, Docket No. 18638-U, Direct Testimony of Charles W. King, page 4.
[31] Id.

Alternatives to TIFCA Approved by Public Service Commissions

> The Commission finds as a matter of fact that the depreciation rates proposed by the Commission's Adversary Staff are fair, just and reasonable.[32]

Although Commissioner Stan Wise dissented with the Commission's Order, he agreed with the Order in the area of depreciation rates.[33] On May 9, 2005, Atlanta Gas Light filed a Petition For Rehearing, Reconsideration and Oral Argument. As of May 11, 2005, the Commission had not responded to that petition.

[32] I/M/O Atlanta Gas Light Company, Docket No. 18638-U, Order, Issued April 27, 2005, page 6.

[33] I/M/O Atlanta Gas Light Company, Docket No. 18638-U, Order, Issued April 27, 2005, Dissenting Opinion of Commissioner Stan Wise, page 2.

Response of the Attorney General to
Initial Data Request of Union Light Heat & Power Company to the Attorney General
Union Light Heat & Power Company
Case No. 2005-00042

Witness Responding: Michael J. Majoros, Jr.

40. Refer to page 21, lines 5-7 of Mr. Majoros' Direct Testimony. Provide all references to Mr. Spanos' testimony, discovery requests and provide all supporting documents for this Mr. Majoros' statement that "[a]ll of Mr. Spanos' net salvage data relates to abandoned services that were not removed and were related to instances where the dwellings were razed."

Response:

Please see Mr. Majoros' testimony, page 20. See also Exhibit___(MJM-11) , specifically page 12 of 13, which is ULH&P's response to AG-DR-02-035.

Response of the Attorney General to
Initial Data Request of Union Light Heat & Power Company to the Attorney General
Union Light Heat & Power Company
Case No. 2005-00042

Witness Responding: Michael J. Majoros, Jr.

41. Refer to page 23, line 18 of Mr. Majoros' Direct Testimony. Provide the case numbers, dates of orders, and copies of the KyPSC orders referred to in this statement.

Response:

See publicly the Orders for Kentucky Utilities Company and Louisville Gas & Electric Company in Case Nos. 2003-00426 and Case No. 2003-00427, issued December 23, 2003 which may be found at the following links.

http://psc.ky.gov/order_vault/2003_Orders/2003_by_case_number/200300426_12232003.doc

for the December 23, 2003 Order in 2003-00426

http://psc.ky.gov/order_vault/2003_Orders/2003_by_case_number/200300427_12232003.doc

for the December 23 Order in 2003-00427

**Response of the Attorney General to
Initial Data Request of Union Light Heat & Power Company to the Attorney General
Union Light Heat & Power Company
Case No. 2005-00042**

Witness Responding: Michael J. Majoros, Jr.

42. Refer to page 23, lines 24-26 of Mr. Majoros' Direct Testimony. Provide the case numbers, dates of orders, and copies of any state utility commission orders where a commission has ordered a utility company to recognize a regulatory liability for non-legal AROs.

Response:

See Florida PSC Order PSC-03-0906-FOF-PU, issued August 7, 2003 in Docket No. 030304-PU, and page 123.4 of FPL's 2004 Form 1 Report identifying the regulatory liability for regulatory purposes. See also FPL response to OPC Interrogatory No. 56 providing further information. All of these documents are attached.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Proposed adoption of Rule 25-14.014, F.A.C., Accounting for Asset Retirement Obligations under SFAS 143.

DOCKET NO. 030304-PU
ORDER NO. PSC-03-0906-FOF-PU
ISSUED: August 7, 2003

The following Commissioners participated in the disposition of this matter:

LILA A. JABER, Chairman
J. TERRY DEASON
BRAULIO L. BAEZ
RUDOLPH "RUDY" BRADLEY
CHARLES M. DAVIDSON

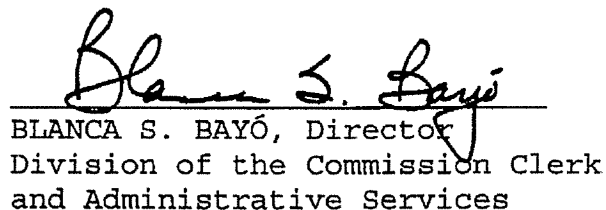
<u>NOTICE OF ADOPTION OF RULE</u>

NOTICE is hereby given that the Florida Public Service Commission, pursuant to Section 120.54, Florida Statutes, has adopted Rule 25-14.014, Florida Administrative Code, relating to accounting for asset retirement obligations under SFAS 143, without changes.

The rule was filed with the Department of State on August 6, 2003 and will be effective on August 26, 2003. A copy of the rule as filed with the Department is attached to this Notice.

This docket is closed upon issuance of this notice.

By ORDER of the Florida Public Service Commission, this 7th day of August, 2003.



BLANCA S. BAYÓ, Director
Division of the Commission Clerk
and Administrative Services

(S E A L)

MKS

DOCUMENT NUMBER-DATE
07240 AUG-7 03
FPSC-COMMISSION CLERK

25-14.014 Accounting for Asset Retirement Obligations Under SFAS 143.

(1) The Financial Accounting Standards Board issued Statement No. 143, Accounting for Asset Retirement Obligations (SFAS 143) in June 2001. The statement applies to legal obligations associated with the retirement of tangible, long-lived assets that result from the acquisition, construction, development or normal operation of a long-lived asset. For utilities required to implement SFAS 143, it shall be implemented in a manner such that the assets, liabilities and expenses created by SFAS 143 and the application of SFAS 143 shall be revenue neutral in the rate making process.

(2) Definitions. For purposes of this rule, the following definitions apply:

(a) "Accretion Expense." The concurrent cost that is recorded as an operating item in the statement of income to account for the passage of time and the resulting period-to-period increase in the Asset Retirement Obligation.

(b) "Asset Retirement Cost." The amount capitalized that increases the carrying amount of the long-lived asset when a liability for an Asset Retirement Obligation is recognized.

(c) "Asset Retirement Obligation." An obligation associated with the retirement of a tangible long-lived asset.

(3) Pursuant to SFAS 143, each utility shall recognize the fair value of a liability for an Asset Retirement Obligation in the period in which it is incurred if a reasonable estimate of the fair value can be made. If a reasonable estimate of fair value cannot be made in the period the Asset Retirement Obligation is incurred, the liability shall be recognized when the reasonable estimate of fair value can be made. The fair value of the liability for an Asset Retirement Obligation is the amount at which that liability could be settled in a current transaction between willing parties, that is, other than in a forced or liquidation transaction. If quoted market prices are not available, the estimate of fair value shall be based on the best information available in the circumstances including prices for similar liabilities and the result of present value or other valuation techniques. The Asset Retirement Obligations shall be kept by function and recorded in separate subaccounts.

(4) Upon initial recognition of a liability for an Asset Retirement Obligation, the utility shall capitalize an Asset Retirement Cost by increasing the carrying amount of the long-lived

assets by the same amount as the liability. The Asset Retirement Cost shall be kept by function and recorded in a separate subaccount as intangible plant. The utility shall subsequently allocate that Asset Retirement Cost to expense over its useful life. The expense shall be recorded in a separate subaccount.

(5) Asset Retirement Costs do not qualify for Allowance for Funds Used During Construction.

(6) Pursuant to SFAS 143, in periods subsequent to the initial measurement, a utility shall recognize period-to-period changes in the liability for an Asset Retirement Obligation resulting from accretion or revisions to either the timing or the amount of the original estimate of undiscounted cash flows.

(a) A utility shall measure the accretion cost in the liability for an Asset Retirement Obligation due to passage of time by applying the interest method of allocation to the amount of the liability at the beginning of the period. This amount shall be recognized as an increase in the carrying amount of the liability.

(b) The accretion expense shall be recorded in a separate subaccount.

(c) Revisions to a previously recorded Asset Retirement Obligation will result from changes in the assumptions used to

estimate the cash flows required to settle the Asset Retirement Obligation, including changes in estimated probabilities, amounts, and timing of the settlement of the Asset Retirement Obligation, as well as changes in the legal requirements of an obligation. Upward revisions to the undiscounted estimated cash flows shall be treated as a new liability and discounted at the current rate. Downward revisions will result in a reduction of the Asset Retirement Obligation. The amount of the liability to be removed shall be discounted at the rate that was used at the time the obligation was originally recorded. The concurrent debit or credit shall be made to the Asset Retirement Cost.

(7) Differences between amounts prescribed by the Commission and those used in the application of SFAS 143 shall be recorded as Regulatory Liabilities or Regulatory Assets in separate subaccounts.

(8) The Regulatory Debit and Regulatory Credit accounts shall be used to record the differences between the Commission prescribed amounts and the amounts which are reported as expense under SFAS 143.

(9) Each utility shall keep records supporting the calculation and the assumptions used in the determination of the

Asset Retirement Obligation and the related Asset Retirement Cost and the related Regulatory Assets and Regulatory Liabilities established in accordance with this rule and the implementation of SFAS 143.

(10) If a utility is not required to establish an Asset Retirement Obligation for an asset or group of assets, the cost of removal shall continue to be included in the calculation of the depreciation expense and accumulated depreciation.

Specific Authority: 350.127(2) F.S.

Law Implemented: 364.03, 364.035, 366.05(1), 367.121(1)(a) F.S.

History: New 08/26/03.

THIS FILING IS	
Item 1: [X] An Initial (Original) Submission	OR [ ] Resubmission No. ____

Form 1 Approved
OMB No. 1902-0021
(Expires 6/30/2007)
Form 1-F Approved
OMB No. 1902-0029
(Expires 6/30/2007)
Form 3-Q Approved
OMB No. 1902-0205
(Expires 6/30/2007)

FERC FINANCIAL REPORT
FERC FORM No. 1: Annual Report of Major Electric Utilities, Licensees and Others and Supplemental Form 3-Q: Quarterly Financial Report

These reports are mandatory under the Federal Power Act, Sections 3, 4(a), 304 and 309, and 18 CFR 141.1 and 141.400. Failure to report may result in criminal fines, civil penalties and other sanctions as provided by law. The Federal Energy Regulatory Commission does not consider these reports to be of confidential nature

Exact Legal Name of Respondent (Company)	Year/Period of Report
Florida Power & Light Company	End of 2004/Q4

FERC FORM No.1/3-Q (REV. 02-04)

Name of Respondent	This Report is:	Date of Report (Mo, Da, Yr)	Year/Period of Report
Florida Power & Light Company	(1) X An Original (2) _ A Resubmission	/ /	2004/Q4

NOTES TO FINANCIAL STATEMENTS (Continued)

commencement of plant operation, these costs are transferred to electric utility plant in service and other property. At December 31, 2004 and 2003, FPL Energy recorded approximately $55 million and $174 million, respectively, of construction accruals, which are included in other current liabilities on FPL Group's consolidated balance sheets.

Asset Retirement Obligations – Effective January 1, 2003, FPL Group and FPL adopted FAS 143, "Accounting for Asset Retirement Obligations." See Note 15.

Decommissioning of Nuclear Plants, Dismantlement of Plants and Other Accrued Asset Removal Costs – Following are the components of FPL Group's and FPL's decommissioning of nuclear plants, dismantlement of plants and other accrued asset removal costs:

	FPL									
	Nuclear Decommissioning		Fossil Dismantlement		Interim Removal Costs		FPL Energy		FPL Group	
	December 31,		December 31,		December 31,		December 31,		December 31,	
	2004	2003	2004	2003	2004	2003	2004	2003	2004	2003
	(millions)									
Asset retirement obligations (ARO)	$ 2,013	$ 1,907	$ 2	$ 1	$ -	$ -	$ 192	$ 178	$ 2,207	$ 2,086
Less capitalized ARO asset net of accumulated depreciation	214	222	1	1	-	-	-	-	215	223
Accrued asset removal costs (a)	158	143	291	274	1,563	1,485	-	-	2,012	1,902
Asset retirement obligation regulatory expense difference (a)	267	181	(1)	(1)	-	-	-	-	266	180
Accrued decommissioning, dismantlement and other accrued asset removal costs	$ 2,224(b)	$ 2,009(b)	$ 291(b)	$ 273(b)	$ 1,563(b)	$ 1,485(b)	$ 192	$ 178	$ 4,270	$ 3,945

(a) Regulatory liability on FPL Group's and FPL's consolidated balance sheets.
(b) Represents total amount accrued for ratemaking purposes.

FPL – For ratemaking purposes, FPL accrues for the cost of end of life retirement and disposal of its nuclear and fossil plants over the expected service life of each unit based on nuclear decommissioning and fossil dismantlement studies periodically filed with the FPSC. In addition, FPL accrues for interim removal costs over the remaining life of the related assets based on depreciation studies approved by the FPSC. Beginning January 1, 2003, FPL began recognizing decommissioning and dismantlement liabilities for financial reporting purposes in accordance with FAS 143, which requires that a liability for the fair value of an ARO be recognized in the period in which it is incurred with the offsetting associated asset retirement cost capitalized as part of the carrying amount of the long-lived asset. Any differences between expense recognized under FAS 143 and the amount recoverable through rates is deferred in accordance with FAS 71. See Electric Plant, Depreciation and Amortization and Note 15.

Nuclear decommissioning studies are performed at least every five years and are submitted to the FPSC for approval. FPL plans to file updated nuclear decommissioning studies in 2005. FPL's latest nuclear decommissioning studies became effective in May 2002 and provide for an annual decommissioning expense accrual of $79 million. These studies assume prompt dismantlement of Turkey Point Units Nos. 3 and 4 with decommissioning activities commencing in 2012 and 2013, respectively, when the original operating licenses are to expire. Current plans, which are consistent with the term of the original operating licenses, call for St. Lucie Unit No. 1 to be mothballed beginning in 2016, with decommissioning activities to be integrated with the prompt dismantlement of St. Lucie Unit No. 2 beginning in 2023. These studies also assume that FPL will be storing spent fuel on site pending removal to a U.S. government facility. The studies indicate FPL's portion of the ultimate costs of decommissioning its four nuclear units, including costs associated with spent fuel storage, to be $6.4 billion. FPL's portion of the ultimate cost of decommissioning its four units, expressed in 2004 dollars, is estimated by the studies to aggregate $2.2 billion.

During 2004, with respect to costs associated with nuclear decommissioning, FPL recognized approximately $106 million related to ARO accretion expense, approximately $8 million related to depreciation of the capitalized ARO asset, approximately $6 million related to the non-legal obligation included in accrued asset removal costs and an approximate $41 million credit to adjust the total accrual to the $79 million approved by the FPSC for decommissioning expense (included in depreciation and amortization expense in FPL Group's and FPL's consolidated statements of income). During 2003, FPL recognized approximately $101 million related to ARO accretion expense, approximately $8 million related to depreciation of the capitalized ARO asset, approximately $6 million related to the non-legal obligation included in accrued asset removal costs and an approximate $36 million credit to adjust the total accrual to the $79 million approved by the FPSC for decommissioning expense. During 2002, FPL accrued decommissioning expense of approximately $81 million, which is included in depreciation and amortization expense.

Restricted trust funds for the payment of future expenditures to decommission FPL's nuclear units are included in special use funds of FPL. Consistent with regulatory treatment, securities held in the decommissioning funds are carried at market value with market adjustments, including any other-than-temporary impairment losses, resulting in a corresponding adjustment to the related liability accounts. See Note 10 – Special Use Funds. Contributions to the funds are based on current period decommissioning

Florida Power & Light Company
Docket No. 050045-EI
Docket No. 050188-EI
Depreciation - OPC's Third Set of Interrogatories
Interrogatory No. 56
Page 1 of 1

Q.

Please refer to Note 1 – Summary of Significant Accounting and Reporting Policies – Decommissioning of Nuclear Plants, Dismantlement of Plants and Other Accrued Asset Removal Costs, in the December 31, 2004 10K Report.
Please provide the related calculations of the amounts included in the table in that section. Please be specific as to what is included in the "Accrued Asset Removal Costs" amounts for Nuclear Decommissioning of $158 million (2004) and $143 million (2003), for Fossil Dismantlement of $291 million (2004) and $274 million (2003), and for Interim Removal Costs of $1.6 billion (2004) and $1.5 billion (2003). Please provide these calculations in electronic format (Excel) with all formulae intact.
The table indicates that the "Accrued Asset Removal Costs" are listed as Regulatory Liabilities on FPL Group's and FPL's consolidated balance sheets. A regulatory liability is an amount owed to ratepayers until it is spent on its intended purpose. Please provide an explanation of how the Company plans to guarantee that these amounts will be spent entirely on asset removal and if not, how the Company intends to return these amounts to ratepayers.

A.

The total amounts reported in the table appearing on the line "Accrued decommissioning, dismantlement and other accrued asset removal cost" represent the total accumulated provision for Nuclear Decommissioning, Fossil Dismantlement and Interim Removal costs calculated and accrued in accordance with applicable Commission rules and prior orders pertaining to accounting for Nuclear Decommissioning, Fossil Dismantlement, and depreciation of utility plant. The amounts appearing on the line "Accrued Asset Removal Costs" represent the estimated accrued asset removal costs calculated in accordance with amounts approved by the Commission for regulatory purposes that do not qualify as a legal obligation or otherwise meet the definition of an Asset Retirement Obligation (ARO) as defined by the accounting requirements of FASB Statement No. 143. For regulatory reporting these amounts are recorded in account 108-accumulated provision for depreciation of electric utility plant. For external financial reporting purposes these amounts are reclassified from account 108 and reported as a regulatory liability. Amounts reported as Interim Removal Costs represent the estimate of accumulated removal costs recorded as depreciation expense that has been recovered through the removal cost component of the depreciation rates approved by the Commission. Interim Removal costs represent one component of the total accumulated provision for depreciation that is evaluated and adjusted prospectively with each review and approval of depreciation rates by the Commission.
Amounts accrued as Decommissioning and Dismantlement are approved on a unit specific basis and are subject to ongoing Commission review and approval. Provided as Attachment 1 to this response are worksheets supporting the table appearing in Note 1. Attachment 2 provided with this response contains the calculation of Interim Removal Costs at December 31, 2004, used in Note1.
FPL is subject to continued regulatory oversight. The Rules and practices of the Commission require that removal cost be accounted for by charging the amount incurred against the accumulated reserve and has approved the depreciation rates of the utility which take into account the accrual of removal cost. The Commission has the oversight on the final disposition of the costs accrued by the utility which are accrued for a specific purpose. Should the assets of the utility be removed and a component of the reserve (including removal cost) remain, the Commission has provided that such amounts can not be transferred or adjusted without Commission approval as stated in Rule 25-6.0436.

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43. Refer to page 24, lines 1-3 of Mr. Majoros' Direct Testimony. Provide the case numbers, dates of orders, and copies of any state utility commission orders where a commission has ordered a utility company to perform separate identification and reporting for regulatory liabilities based on non-legal AROs.

Response:

See Mr. Majoros' response to Question No. 42. Also, see the discussion of Missouri Case No. GR-99-315 involving Laclede Gas Company, in the attachment provided in response to Question No. 39.

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44. Refer to page 31, line 9 – page 32, line 20 of Mr. Majoros' Direct Testimony. Provide examples of any electric utilities operating in states where retail electric generation has not been deregulated, where the utility recognized past collections of costs of removal as income.

Response:

Mr. Majoros has no specific examples of this at this time. That does not mean they do not exist. Mr. Majoros is not a member of EEI. That would probably be the best place to look for this answer.

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45. Refer to page 34, lines 26-28 of Mr. Majoros' Direct Testimony. Provide the basis for this statement.

Response:

See Mr. Majoros' response to Staff Data Request No. 1-22.

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46. Refer to page 35, lines 1-4 of Mr. Majoros' Direct Testimony. Provide the basis for this statement that ratepayers have a "security interest" in "these monies" relating to cost of removal of non-legal AROs.

Response:

Mr. Majoros is not an attorney and does not profess to be one. However, he does recall the business law courses he took in college. One of his texts was Business Law, by John W. Wyatt and Madie B. Wyatt[1]. Chapter 36 is titled "The Security Interest." The first paragraph of Chapter 36 states:

> A security interest means an interest in personal property which secures payment or performance of an obligation. The four things which should be discussed are (1) the agreement creating the security interest, (2) the attachment of the security interest, (3) the perfection of the security interest, and (4) the rights and duties of the parties with respect to the collateral.[2]

The first paragraph of the section titled "Perfection of the Security Interest" also states:

> The purpose of perfecting a security interest is to give the secured party a superior position over certain other lien creditors with respect to the collateral. The secured party may protect his security interest in three ways: (1) By taking physical possession of the collateral; (2) by filing a financing statement, and (3) by attachment alone in some instances. The methods of perfection are set out in sections 9-304 and 9-305, and are determined by the classification of the collateral. It seems appropriate, therefore, to discuss the methods of perfection by class of collateral.[3]

These are the concepts, "security interest" and "perfection of the security interest," Mr. Majoros had in mind when he wrote his testimony. As explained in his testimony, Mr. Majoros believes that ULH&P may have the incentive to somehow relieve itself of the regulatory liability to the detriment of ratepayers and thus resulting in a "windfall" for

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[1] John W. Wyatt, S.J.D. and Madie B. Wyatt, A.B., LL.B., Business Law, 3rd Ed., McGraw-Hill, 1996.
[2] Id., page 478.
[3] Id., pages 479-480.

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management and possibly shareholders. Cinergy has already done that, as well as AEP and TEP, among other electric utilities. It is also what the telephone industry did. Confirming ratepayers' security interest will serve to eliminate any potential confusion about the future disposition of these excess collections, should they not be spent on removal costs.

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47. On page 8 of 40 of his Direct Testimony, Mr. Majoros provides a summary of the plant types for which he disagrees with ULH&P's proposed depreciation rates. For each plant type in that list, provide the case numbers and jurisdiction for each proceeding in which Mr. Majoros has made recommendations for these plant types during the past ten years, and provide Mr. Majoros' specific recommendations regarding such plant types in those cases. For each recommendation, indicate whether the commission in that proceeding approved or disapproved Mr. Majoros' recommended ASL/Survivor Curve type and his net salvage value.

Response:

Mr. Majoros has not conducted such an analysis.

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48. The text of Mr. Majoros' testimony is numbered 1 through 38 of 40. Please confirm that the numbering was in error, and that Mr. Majoros' testimony only consists of 38 pages. In the alternative, please provide the missing pages.

Response:

The numbering is in error. Mr. Majoros' testimony consists of 39 pages, one of which is the cover page.

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49. To the extent the Commission approves the proposed reduction to depreciation expense advocated in Mr. Majoros' testimony, does Mr. Majoros agree that the net utility plant used as the basis for calculating the rate base ratio should be adjusted as well?

Response:

No.

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50. Regarding your recommendation that the Commission should require ULH&P to establish a regulatory liability for any costs of removal for non-legal AROs, please state:

   a. do you agree that your recommendation is based, in part, on the fact that CG&E has treated as income such costs related to the three plants it is transferring to ULH&P;

   b. do you have any indication that ULH&P or PSI have treated as income any costs of removal for non-legal AROs?

   c. do you agree that retail electric generation service is deregulated in Ohio, and that this may be the basis for CG&E to treat such costs as income;

Response:

a. Your premise is incorrect. Mr. Majoros recommends that the Commission recognize the regulatory liability that already has been established. Mr. Majoros would have made this recommendation regardless of the transferred plants. However, they do seem to bolster the need for regulatory recognition of the regulatory liability.

b. No.

c. Mr. Majoros is not an expert on Ohio regulation. Furthermore, regardless of that, CG&E relieved itself of a liability without having to pay.

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51. Please provide a copy of your testimony in Case No. 2003-00434.

Response:

Please see the direct testimony of Michael J. Majoros, Jr. filed in three parts in Case No. 2003-00434 at the following links.

http://psc.ky.gov/pscscf/2003-00434/AG_Testimony_MichaelJMajorosJr_Testimony_Depreciation_032304.pdf

Testimony concerning Depreciation filed in 2003-00434

http://psc.ky.gov/pscscf/2003-00433/AG_Testimony_MichaelJMajorosJr_032304.pdf

Testimony concerning SFAS 143 filed in 2003-00434 as well as in LG&E's case No. 2003-00433, but available on the website only in the LG&E case compilation of non-electronic filings.

http://psc.ky.gov/pscscf/2003-00434/AG_Testimony_MichaelJMajorosJr_032304.pdf

Testimony concerning revenue requirements filed in KU 2003-00434

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52. Provide a copy of any KyPSC decision expressly discussing the Normalized Net Salvage Allowance Accrual Approach referenced on page 6 of Exhibit MJM-13.

Response:

Please see the May 21, 2001 Order for Jackson Energy Cooperative Corporation (Case No. 2000-373), the August 7, 2002 Order for Fleming-Mason Energy Cooperative Corporation (Case No. 2001-00244), the June 30, 2004 and August 12, 2004 Orders for Kentucky Utilities Company/Louisville Gas & Electric Company (Case Nos. 2003-00433 and 00434) and the November 10, 2004 Order for Delta Natural Gas Company (Case No. 2004-00067) which area available at the following links.

Though noted on the Order as being issued on May 21, 2001, the Jackson Energy Cooperative Corporation Order for Case No. 2000-00373 appears on the PSC website on June 5, 2001
http://psc.ky.gov/order_vault/2001_Orders/2001_By_Case_Number/2000373_052101.doc

August 7, 2002 Order in Fleming-Mason Energy Cooperative Corporation
http://psc.ky.gov/order_vault/2002_Orders/2002_By_Case_Number/200100244_080702.doc

June 30, 2004 Order in 2003-00433 LG&E
http://psc.ky.gov/order_vault/2004_0rders/2004_by_case_number/200300433_06302004.pdf

August 12, 2004 Order in 2003-00433 LG&E
http://psc.ky.gov/order_vault/2004_0rders/2004_by_case_number/200300433_08122004_3.doc

June 30, 2004 Order in 2004-00434 KU
http://psc.ky.gov/order_vault/2004_0rders/2004_by_case_number/200300434_06302004.pdf

August 12, 2004 Order in 2004-00434 KU
http://psc.ky.gov/order_vault/2004_0rders/2004_by_case_number/200300434_08122004_3.doc

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Though dated November 10, 2004, the Order for Delta Natural Gas appears on the PSC website on November 16, 2004
http://psc.ky.gov/order_vault/2004_0rders/2004_by_case_number/200400067_11102004.doc

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53. Provide the case numbers, dates of orders, and copies of any state utility commission orders where a commission has expressly adopted a Cash Basis Alternative to TIFCA.

Response:

Please see references to the Missouri Laclede Gas Company and Empire District Electric Company and the Oklahoma Empire District Electric Company cases in the document provided with Mr. Majoros' response to Question No. 39.

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54. Provide the case numbers, dates of orders, and copies of any state utility commission orders where a commission has expressly adopted the Net Salvage Allowance Accrual Approach.

Response:

Please see references to the New Jersey Rockland Electric Company and Jersey Central Power & Light Company cases, the Pennsylvania approach, and the Kentucky Jackson Energy Cooperative and Fleming-Mason Energy Cooperative Corporation cases in the attachment to the response to Question No. 39.

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55. Provide the case numbers, dates of orders, and copies of any state utility commission orders where a commission has expressly adopted the SFAS No. 143 Fair Value Accrual Approach.

Response:

See references to SFAS No. 143 in New Jersey decisions discussed in the attachment to the response to Question No. 39. Also, see the "separation" discussions in the Central Vermont Public Service Company and the Georgia Power Company Docket No. 18300-U and Atlanta Gas Light Company Docket 18638-U.

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56. Provide the case numbers, dates of orders, and copies of any state utility commission orders where a commission has expressly adopted the Net Present Value Accrual Approach.

Response:

See references to the Georgia Power Company and the Atlanta Gas Light Company cases in the attachment provided in response to Question No. 39.

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Witness Responding: Dr. J. Randall Woolridge

57. At page 8, line 18 of his testimony, Dr. Woolridge, uses a long-term debt rate of 6.302%. At page 9, lines 17-18 of his testimony, Dr. Woolridge, uses a long-term debt rate of 5.926%. Please identify the source information and provide the workpapers Dr. Woolridge used to develop the long-term debt rate of 5.926%.

Response:

Schedule J-3, page 2 shows that the Company's proposed embedded cost of long term debt for the forecasted period of 6.302% incorporates a cost rate of 6.77% for the $73.3 million Inter-Company Note. However, in its responses to PSC-3-9 and PSC-3-16, the Company concedes that this cost rate should be changed to 5.50%. The overall embedded cost of long term debt with the 5.50% rate rather than the 6.77% rate provides a revised overall cost of long term debt of 5.926%.

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Witness Responding: Dr. J. Randall Woolridge

58. Please provide copies of the relevant pages from the C.A. Turner Utility Reports and/or the Value Line Investment Surveys used in the development of figures shown in JRW-3.

Response:

See response to PSC-I-26 provided on CD.

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Witness Responding: Dr. J. Randall Woolridge

59. In each rate proceeding for which you have submitted testimony since 2000, please provide the name of the utility; the name of the state commission; the case number; your recommended ROE and the ROE adopted by the state commission.

Response:

Company	Docket No.	Date	Recommend	10-Year Yield	Adoption
PSWC	00994868	Feb 2000	9.0%	6.68%	Unknown
Artesian	00-649	April 2001	10.0%	5.67	Unknown
PAWC	00016339	August 2001	9.0%	5.06	
Wellsboro Elec	00016356	Nov 2001	9.75%	5.15	Unknown
PSWC	00016750	Feb 2002	9.0%	5.30	Unknown
NFG	0038168	July 2003	9.1%	4.61	Unknown
PAWC	0038304	August 2003	8.4%	4.66	10.60%
SBC Ohio	02-1280	May 2004	10.0%	4.03	10.0%
York Water	00038304	July 2004	8.75%	4.59	Unknown
Ken-American	2004-0103	August 2004	8.75%	4.22	10.0%
Yankee Gas	04-06-01	Sept 2004	8.75%	4.23	Unknown
Cen Vermont	6446	Oct 2004	8.75%	4.14	10.0%
Valley Energy	00040345	Nov 2004	9.0%	4.44	Unknown
NFG	00049656	Dec 2004	8.50%	4.30	Unlnown
Wellsboro Elec	00049313	Dec 2004	9.0%	4.30	Unknown

Most 'Unknown' case decisions were settlements.

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Witness Responding: Dr. J. Randall Woolridge

60 a) Please provide the currently authorized return on equity for the each of the eleven natural gas utilities in your sample of comparable companies shown on Exhibits JRW-3-1 and JRW-7-2.

b) Are there any investor-owned natural gas utilities with an allowed rate of return on common equity that is equal to, or less than, what Mr. Woolridge recommends in this proceeding? If so, provide a list of such utilities.

Response:

a) See 'Allowed ROE' data provided in CA Turner Utility Reports for May, 2005, as provided in response to PSC-I-26 on CD.

b) No, but Dr. Woolridge is not aware of the results of all gas rate cases.