Accounting – Technical Releases

TR1, 2, 3, 4, 5, 6, 7, 8, 10 and 16

NEW YORK STATE PUBLIC SERVICE COMMISSION

TECHNICAL RELEASES

ON

ACCOUNTING, FINANCE AND RATE

MATTERS

By the
Director of Accounting and Tariff Analysis

FOREWORD

Technical releases are informal explanations or interpretations of the Uniform Systems of Accounts, of financing and ratemaking requirements and of related matters. These releases are to be followed in the absence of specific references in the prescribed regulations and other authoritative decisions of the Commission.

These releases represent the opinions of the Director of Accounting and Tariff Analysis on selected accounting, financing and ratemaking matters.

The releases are numbered consecutively and are followed by one or more of the letters E, G, S, T, or W denoting that the interpretation is applicable to electric, gas, steam, telephone or water-works companies.

Additional releases will be issued from time to time as they appear necessary. Individual requests for interpretations and explanations will be handled on an ad hoc basis and are encouraged when there is an element of uncertainty.

Technical Release Number 1
(Effective Immediately)
Class A and B Utilities

Question:

There are occasions when an unusual item of an extraordinary nature is relatively so large in amount that its inclusion in the expense accounts for the year in which the transaction occurred would seriously distort operating results. In some cases it may be appropriate to amortize such an item over a future period. When such occasions occur what action should the company take?

Answer:

As specified in General Instruction 166.17[1/] of the Uniform System of Accounts for Electric Corporations, Commission approval is required to defer expense items beyond the year in which the transaction occurred. The company should file a petition with the Commission as early during the year as possible but prior to the

1/ Gas Corporations - Section 311.7; Steam Corporations Section 461.14; Telephone Corporations - Section 661 Water Works Corporations - Section 561.18.

end of year, requesting permission to defer the item together with a plan of amortization.

The petitioner should file with its petition:

(1) An explanation of the item for which deferral and amortization is requested, including the nature of the item, the accounts in which the items would normally be included, and the reason(s) for deferral and amortization.

(2) Detailed income statements for the most recent two years. For example, income statements filed with a petition on June 15 should be for the periods ending May 31. If this imposes a hardship, the petitioner, with adequate justification, may file income statements for the periods ending April 30.

(3) Detailed balance sheets for the years ended the dates of the income statements required in (2) above.

(4) The estimated federal income tax effect of the item or transaction for which deferral is requested.

(5) The period over which and the accounts to which the deferred item is to be charged in future periods.

EVERETT L. MORRIS
Director of Accounting and
Tariff Analysis

Issued:

June 30, 1972

TR-1

Technical Release Number 2
(Effective Immediately)
Class A and B Utilities

Question:

The Uniform System of Accounts permits companies to capitalize interest on construction but does not provide specific guidance on the rate to use.

What is the proper rate for a utility to use for capitalization of interest during construction and when is it appropriate to change the rate?

Answer:

The rate for capitalization of interest during construction should not exceed the rate of return allowed the utility in its most recent rate case. If a utility considers the most recently allowed rate of return too low for present circumstances it should request approval of the Director of Accounting and Tariff Analysis to increase its rate. At the time of the request to change the rate the utility should submit full justification in support of its request.

Depending on the level of short term interest rates and other factors the appropriate rate for capitalization of interest may well be below the allowed rate of return. Therefore, it does not necessarily follow that an immediate increase in the interest capitalization rate is justified when a higher rate of return is authorized by the Commission. The rate used to capitalize interest should not be increased without the approval of the Director of Accounting and Tariff Analysis

EVERETT L. MORRIS
Director of Accounting and
Tariff Analysis

Issued:

June 30, 1972

TR-2

Technical Release Number 3
(Effective Immediately)
Class A and B Utilities

Question:

Part 48, Article 4, Subchapter C of the Rules of Procedure specifies the data which must be filed with all financing petitions. The use of leases as financing instruments appears to be increasing and the data filed with a normal debt or stock financing petition is usually not sufficient for an evaluation of a lease proposal. What supplementary information, in addition to that required by the Rules of Procedure for a financing petition, is required to be filed with a petition requesting approval of a lease as a financing instrument?

Answer:

One critical element in evaluation of a lease proposal is the cost comparison - that is, the cost of the proposed lease compared with the alternative cost of ownership.

Two assumptions can be made about the cost of financing when the cost of ownership is being analyzed. (Changes in accounting requirements could affect such assumptions). It can presently be assumed that ownership is achieved first, by debt at the incremental cost and second, by the composite capitalization, using current costs for fixed capital and the most recently allowed return on the common equity component.

In making the analysis all quantifiable factors should be measured including any values resulting from benefits available under the tax laws. The present value of cash flow or cash requirements is important in evaluating benefits or costs under different alternatives. Applicants are encouraged to fully explore, analyze, and explain the non-quantifiable factors pertaining to the lease proposal.

In addition to the data currently required by the Rules of Procedure for financing petitions, all lease proposals shall include a

TR-3

detailed comparison of the cost of the proposed lease versus the cost of ownership under the two assumptions discussed above. The cost comparison shall include appropriate time values.

EVERETT L. MORRIS
Director of Accounting and
Tariff Analysis

Issued:

June 30, 1972

TR-3

(EGSTW)

TECHNICAL RELEASE NUMBER 4
(EFFECTIVE IMMEDIATELY)
CLASS A AND B UTILITIES

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

APPROVED BY THE COMMISSION OCT 24 1972

October 16, 1972

TO: THE COMMISSION

FROM: DIRECTOR, OFFICE OF ACCOUNTING AND TARIFF ANALYSIS (Acting)

SUBJECT: Rate at which to capitalize interest during construction

* * *

Four letters objecting to Technical Release Number 2, which deals with the rate to be used for capitalizing interes during construction, have been received. The first three releases of an intended continuing series (Technical Releases o ccounting, Finance and Rate Matters) were distributed as of une 30, 1972 over the signature of Everett Morris, Director Accounting and Tariff Analysis.

The four respondents objecting to Release Number 2 are Naylon, Huber, MaGill, Lawrence & Farrell*, Long Island Light Niagara Mohawk, and Central Hudson. All four welcome the publication of the Technical Releases, and find Numbers 1 and 3 useful and informative. Number 1 deals in greater detail tha the rules of procedure with material to be filed with request for special accounting, and Number 3 deals with material to b filed in applications for approval of leases.

*A law firm which represents Rochester Gas and Electric, New State Electric and Gas, and Long Island Water in rate procee ings. The law firm, however, makes no representation that i acting in behalf of any client in the letter under discussic

Technical Release Number 2 (attached hereto)* in essence limits the rate at which interest may be capitalized to the rate of return allowed in the utility's last rate proceeding unless the permission of the Director of Accounting and Tariff Analysis is first obtained for a higher rate. Further, the Release requires such permission for any increase in the rate.

All four respondents object to the requirement for the Director of Accounting and Tariff Analysis' prior approval and two of the respondents characterize it as inappropriate rulemaking by the Director of Accounting. Long Island Lighting, Central Hudson, and Niagara Mohawk point out that they would have no objection to notifying the Commission or the Director of Accounting and Tariff Analysis of a change in rate.

Long Island Lighting, Central Hudson, and Niagara Mohawk also object to the standard for determining the rate at which interest may be capitalized. They think it should be the current cost of construction funds. Naylon, Huber, MaGill, Lawrence & Farrell call attention to the Commission's Opinion and Order No. 72-7 (A) issued June 7, 1972 in Case 26112 in which the Commission reaffirmed treatment of interest during construction different from the book treat-

*Refer to page 4 for Technical Release Number 2.

ment, even though the book treatment accorded with the written guidance of the Director of Accounting.

DISCUSSION

Intent of Releases

The releases were intended to clarify the Uniform System of Accounts and other Commission rules and policies related to accounting, finance and rate matters, and to give the staff position on matters on which the Director's opinion is frequently asked or on which frequent variation from what staff considers proper treatment are found because of a diversity in interpretation. It was intended that companies who did not agree with the Director's interpretation would be able to continue their practices, but that they would do so with an awareness of the staff's position and the risk of being challenged and having to defend their treatment to the Commission.

Intent of Technical Release Number 2

The intent of Accounting Release Number 2 is to set standard which would limit the amount of interest being capitalized to a reasonable level, and at the same time gi guidance to companies which are overly conservative, and, therefore, capitalize at too low a rate. Utilities freque claim in rate cases through various mechanisms, an allowan for an amount of return equal to the difference between th interest actually capitalized and the full rate of return on construction work in progress. However, if the company position is accepted, and it has capitalized interest at too low a rate, the adjustment will result in greater rate relief for that company than for similarly situated companies who have used a more appropriate rate. Should the rate at which interest is capitalized be raised subsequently, any rate relief related to capitalizing interest at too low a rate would still continue.

There was, however, no intent that companies should change if they have followed a consistent policy of not capitalizing interest or of consistently excluding certain portions of their construction program from amounts on which interest is capitalized, or have consistently followed simplified procedures.*

Standard for Rate at which Interest is Capitalized

There has never been agreement on criteria for a proper rate at which to capitalize interest. Basically there are two theoretical approaches:

1. Current Cost of Construction Funds. Under this theory the cost of construction funds is viewed like any other cost which is capitalized, and the cost of funds during the construction period is viewed as the cost to be capitalized. There are

* For example, charging one month's interest when a designa class of work orders below certain amounts are closed.

two difficulties with this approach if it is rigidly applied. One is that the cost of permanent capital raised during the construction period is not necessarily related to the construction in that period. A utility typically alternates between common equity, preferred stoc and debt in its security issues. Medium size utilities often have no more than one security issue a year. Under such circumstances, can one say that the cost of new permanent capital used for construction was 7-1/2 percent last year because debt was issued, and 12 percent this yea because equity was issued?

The second difficulty arises in a period suc as 1970 when the cost of short-term capital is well above any conceivable rate of return which the utility may be allowed. Applying the curren cost concept would result in interest being capitalized at a rate in excess of the rate of return. While this may be the cost of construct funds, it appears improper to impute a higher ra of earnings to plant while it is under construct than would be allowed when it is in service. On the other hand, if short-term notes are excluded from the capital structure, the utility will not be compensated for the excess of the cost of short-term money over the rate of return.

2. Historical Cost of Money. This theory views construction funds as the composite of all utility funds. The theory ignores that short-term funds at a different cost than the rate of return may have been used for construction. There would be a logical difficulty, however, if recognition is given to the cost of short-term funds when they are lower than the rate of return, but, for the reason stated above, not when they are higher.

The approach in Technical Release Number 2 envisages a combination of those two perspectives, and is a reasonable and practical one. Further explanation may be warranted concerning the standard generally to be applied.

Construction funds normally are derived from both short-term borrowings and permanent financings. (The amount of permanent capital for this purpose would be the difference between the estimated average balance of construction work in progress and the average balance of short-term funds used for construction purposes.) The interest.rate employed for capitalizing interest during construction should approximate the weighted average of the two sources of funds.

The cost of short-term debt will vary from time to time with fluctuations in the money markets. The cost of permanent financing also will vary as new securities are sold. It is proposed that, for purposes of computing the cost of the permanent financing component of the interest rate to be used in capitalizing interest during constructio the utility employ the cost of equity last found reasonable by the Commission, the current embedded cost of debt and preferred stock, and the utility's current capital structu (unless the Commission's most recent opinion indicated some other capital structure should be used, or employed a "doul leverage" approach, in which case the approach and assumpti of the Commission should be utilized).

If, for example, a utility is capitalized with 55 pe cent long-term debt at 6 percent, 10 percent preferred sto at 7.5 percent, and 35 percent common stock, and if in the last rate case a return of 12 percent on common equity was found to be reasonable, and if the utility is financing con struction projects 60 percent from permanent financings an 40 percent from short-term borrowings at 5.5 percent, the interest rate employed in capitalizing interest during con struction should approximate:

60 percent x	55 percent x	6 percent	=	1.98
60 percent x	10 percent x	7.5 percent	=	0.45
60 percent x	35 percent x	12 percent	=	2.52
40 percent x		5.5 percent	=	2.20
				7.15 percen

In most instances, this approach should yield a rate for capitalizing interest during construction at less than the overall rate of return allowed in the preceding rate case, and, in all likelihood, lower than the overall rate of return which would be permitted in a subsequent rate case. The Director of Accounting and Tariff Analysis or the Commission could give permission to a utility to use a rate higher than the expected overall rate of return when special circumstances warrant, such as a very sharp upturn in short-term interest rates. Also, the special circumstances of a particular utility may warrant a wholly different approach than the one here proposed. Companies which have had no rate proceedings decided during the two years preceding the month in which the rate for capitalizing interest is intended to be increased, can base their computation on comparable companies which have had rate cases decided. But before interest during construction is permitted to be capitalized at a rate higher than the anticipated overall rate of return that probably would be permitted the utility, strong justification should be shown.

<u>Procedure for Changing Rate at which Interest is Charged to Construction</u>

The objectives of Accounting Release Number 2 can be equally well achieved with advance notification (say thirty days) by the utilities as with advance approval. The Directo of Accounting and Tariff Analysis would then be in a position to negotiate about changes with which he disagrees. If agreement cannot be reached, the matter can be referred to the Commission for resolution. While the matter is pending, the utility would be free to capitalize interest at the rate it chooses, but at the risk of having to make appropriate adjustments if the Commission agrees with the Director of Accountin and Tariff Analysis. A similar procedure can be employed for changes proposed by the Director of Accounting and Tariff Analysis.

The Director of Accounting and Tariff Analysis would respond during the thirty day notice period if he had any objection to the rate proposed for capitalizing interest. Failure of the Director to respond would be taken as an indication that he does not elect to object to the rate proposed. but it would not necessarily imply agreement with the method or the figures used to arrive at that rate. The Director would also be free at any time (as he always has been) to suggest that rates at which interest is capitalized should be reduced if a change in underlying conditions warrants it.

However, this procedure places the burden on the staf to prove that a rate of capitalizing interest is not justifi and as a practical matter, would require the staff to arrive at and propose an appropriate rate to the Commission. But, it may be possible to justify a number of appropriate rates within a certain range.

To allow some flexibility to the utilities to adjust their rates for capitalizing interest as conditions change and to keep the staff fully informed of the utility's practices, it may be best that the advance notification procedure outlined above be adopted for all changes (up or down) in the rate for capitalizing interest which do not result in a rate greater than the allowed rate of return in the utility's most recent rate case. The notification should include justification which is in harmony with the approach outlined in this report for arriving at a rate for capitalizing interest.

For increases in the rate for capitalizing interest above the allowed rate of return in the utility's last rate case, advance approval of the Director of Accounting and Tariff Analysis should be obtained because such rates are more likely to be controversial. If the utility wishes to appeal from the Director's ruling, it should justify to the Commission the rate it wishes to use. In view of the objections received to advance approval by the Director of Accounting and Tariff Analysis, it would be desirable for the Commission to formally delegate authority to him to rule on the rate for capitalizing interest under these circumstances.

CONCLUSION AND RECOMMENDATION

It is recommended that the Commission delegate to the [D]irector of Accounting and Tariff Analysis authority to requir[e] advance notification according to the procedures described in this report for all changes in the rate at which interest is capitalized and to require that his approval be obtained befo[re] the rate used to capitalize interest can be increased to a rate higher than the rate of return allowed the utility in it[s] most recent rate case. His ruling would, of course, be subje[ct] to appeal to the Commission.

This report discusses in greater detail than Technical Release Number 2 the guidelines and theory regarding the [d]etermination of an appropriate rate to use for capitalizing interest during construction. It is, therefore, also recommended that the Commission approve its publication as Technic[al] Release Number 4.

Respectfully submitted,

ERIC A. LEIGHTON

Attachment

EAL:kk

APPROVED AS TO FORM

(GE)

ADDENDUM
TO
TECHNICAL RELEASE NUMBER 4

APPROVED BY THE COMMISSION APR 17 1979

Subsequent to this Commission's approval of Technical Release Number 4 the Federal Power Commission, now the Federal Energy Regulatory Commission (FERC) adopted a method to be used by gas and electric utilities under its jurisdiction to determine the rate to be applied in computing an annual allowance for funds used during construction (AFC). While the FERC method and the method prescribed in Technical Release Number 4 use the same approach, there is a difference in the cost of money and capitalization ratios to be used in each method. Simply stated, the difference is really one of timing. Generally, the cost of money and capitalization ratios prescribed for the FERC computation are historical, whereas this Commission's computation is prospective. The exception is short-term debt which is prospective in both methods. Over a period of time, however, both methods will yield essentially the same results.

We understand that FERC insists that their method be used for financial statement purposes and that the Securities and Exchange Commission takes the same view. Since it would be impractical and confusing to require one method to be used for this Commission's ratemaking and reporting purposes and another method for financial statements published by New York State gas and electric utilities subject to FERC jurisdiction, this Commission will allow such utilities to use the FERC method in determining their rate to be applied in computing an annual allowance for funds used during construction provided that such utilities formally notify the Commission in writing that they elect to do so by December 31, 1979 and that they will consistently follow the FERC method in the years thereafter.

The procedure for changing the AFC rate described in Technical Release Number 4 will remain unchanged.

ERIC A. LEIGHTON, Director
Office of Accounting and
Utility Finance

Issued:

(E)

Technical Release Number 5
(Effective Immediately)
Class A and B Electric Utilities

Question:

In connection with the "Statement of Commissic Policy Concerning Fuel Adjustment Clauses of Electric Utilities" issued on January 7, 1974, what is the impact on Financial Reporting for the year ended December 31, 1973 and thereafter?

Answer:

If a utility adopted the Commission policy in respect to Fuel Adjustment Clauses, or had previously applied for and received permission to adopt accounting essentially similar to that authorized in the policy, it should then recognize that a mismatching of revenues and expenses has occured in prior months and, therefore, net income has not been charged with costs related to revenu reflected in the current period. If the amount of such costs, net of taxes, is in excess of 5% of net income fo the current period, then Financial Statements should reflect these amounts separately in the Income Statement. The Uniform System of Accounts does not provide accounts for such a transaction, therefore, utilities should be guided by Opinion 20, Accounting Changes, of the Accounting Principles Board. This Opinion provides that the amounts related to this type of transaction be reported in the financial statements between the captions "Income Before Extraordinary Items" and "Net Income". The amount should be computed in accordance with APB 20, and all financial data submitted by the utility to this Commission should follow the reporting requirements of APB 20.

ERIC A. LEIGHTON, Director,
Office of Accounting and
Tariff Analysis

Issued:

January 14, 1974

TR-5

Technical Release Number 6
(Effective Immediately)
(Class A and B Electric Utilities)

Question:

In what account shall expenditures be included which are made in contemplation of construction of electric utility plant requiring certification under Article VIII of the Public Service Law?

Answer:

Expenditures made in contemplation of constructio[n] of electric utility plant requiring certification under Article VIII of the Public Service Law are required to be made at more than one site before a particular plant can be certified. Before certification it is not possible to tell with certainty whether expenditures at a particular site will result in construction of a plant. However, rejection of a particular site is useful in achieving certification of an alternate site because it narrows the number of remaining choices. All prudent expenditures incurred for certification under Article VIII are, therefore, a necessar[y] part of the cost of construction of the plant eventually certified. Such costs are, therefore, properly chargeable to account 107, Construction Work in Progress - Electric, when incurred. Amounts included in the account are subject to the capitalization of an allowance for funds used during construction and such amounts should be afforded the same accounting treatment as all other construction work in progress expenditures. This method of accounting will compensate utilities for the use of their funds for such expenditures.

Since the submission of more than one building site for an electric generating plant is required,* the accounting for expenditures related to the consideration of several sites must be clarified. For instance, expenditures are incurred for sites A and B, and site A is selected as the building site. The expenditures for both, A and B, become the costs of site A. Further, at a later date, ex-

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* In using the term "required" we mean nothing different from the Commission's "Statement of Policy" accompanying the "Rules of Procedure-Certificates of Environmental Compatibility and Public Need for Major Steam Electric Generating Facilities" issued June 4, 1973 which contains the following sentence: "Thus, while the regulations do not in absolute terms mandate that each application contain full documentation supporting viable facilities at more than one site, any utility not making a bona fide attempt to present meaningful alternatives to the Board would not only be acting at its own peril as to obtaining approval as to any site, but would also run the risk that monies expended for such a faulty presentation would be disallowed as improvident expenditure in a rate case."

penditures are incurred for sites B,[1] C and D, and site C is selected as the building site. The expenditures of B,[1] C and D become the costs of site C. Even if site D were completely ruled out, the expenditures incurred for site D become the costs of the site finally selected, site C.

To avoid capitalization of ongoing engineering, environmental, and similar costs, this accounting applies only to preliminary expenditures related to an electric generating plant requiring certification under Article VIII It is not intended to include the cost of environmental or other studies unless the studies are related to evidence intended to be presented in a proceeding under Article VIII

ERIC A. LEIGHTON, Director,
Office of Accounting and
Utility Finance

Issued:

December 11, 1974

1/ For site B these would include only expenditures in addition to those already incurred and charged to Plant A.

Technical Release Number 7
(Effective Immediately)
Class A and B Utilities

Question:

In computing the allowance for funds used during construction (AFUDC) is it proper for utilities to include AFUDC capitalized in the past in determining the construction costs upon which AFUDC is calculated?

Answer:

Most utilities have been excluding the accumulated AFUDC from the construction costs upon which AFUDC is calculated.

The Commission considered this policy in Case 26552 - Long Island Lighting Company - Electric Rates and in its Opinion No. 75-1 issued in this proceeding on January 9, 1975 stated that:

> "Lastly, we conclude that the policy of not calculating IDC* on that portion of construction work in progress repre-

*IDC stands for "interest during construction". It is still a commonly used abbreviation for what is now called "Allowance for funds used during construction". Whenever the abbreviation IDC appears in the above quotation AFUDC may be substituted without a change of meaning.

sented by past IDC accruals should be reevaluated. In fact, utilities do incur additional capital costs on accrued IDC. In the past, when interest rates were lower, construction budgets smaller and construction periods shorter, the cost of financing accrued IDC may have been minimal. At present, this is not the case. LILCO's test year average IDC approximated $13.5 million; carrying charges on this total would have been more than $1 million. We conclude that it is no longer proper to continue an accounting practice which, in effect, ignores what is now a substantial element of construction costs. Accordingly, LILCO may revise its accounting practices so that in the future IDC will be taken on the entire balance of interest bearing construction work in progress, including accrued interest. This change, if made, will be entirely prospective in nature and will have no impact on the rates approved in this proceeding."

Although in the above quotation permission to revise accounting practices appears to be directed specificall to LILCO, other utilities may make similar revisions effective with interest capitalized in January 1975.

ERIC A. LEIGHTON, Director,
Office of Accounting and
Utility Finance

Issued:

January 28, 1975

TR-7

Technical Release Number 8
(Effective September 1, 1975)
Class A and B Utilities

APPROVED BY THE COMMISSION MAY 28 1975

Question:

What is the accounting required to implement the Gas Adjustment Clause Surcharge or Refund under Section 270.57(f) of Title 16NYCRR? 1/

Answer:

Beginning in September 1975 the month in which the initial determination period would commence under Section 270.57(f) of Title 16NYCRR, gas utilities shall establish a new subdivision of Account 186, Miscellaneous Deferred Debits to be entitled "GAC Surcharge or Refund Adjustment Deferred". In any month in which it is determined that gas costs recoverable through the Gas Adjustment Clause (GAC) exceed GAC revenues, the amount of such excess costs shall be debited to the new subaccount under Account 186 and concurrently credited to the appropriate

1/ See Commission Opinion No. 75-10 issued May 1, 1975 for opinion and resolution adopting this resolution.

subdivisions of the utilities manufactured or purchased gas expense accounts in which the costs were recorded. If in any month GAC revenues exceed gas costs recoverable through the GAC, Account 186 shall be credited with an amount equivalent to the excess of such revenues and the appropriate subdivisions of the utilities manufactured or purchased gas expense accounts shall be concurrently debited with such amount.

The amount remaining in Account 186 at August 31 of each year shall be adjusted to reflect the results of the determination period computation required to be submitted by the utility on October 15th of each year.

Starting with the first billing cycle in December of each year and continuing through the last billing cycle in November in the year following, the amount deferred in Account 186 shall be amortized through charges or credits to the gas expense subaccounts, in amounts equivalent to the surcharge or refund included in GAC revenues booked during each month of this period.

The Federal income tax effect related to the expense amount deferred in Account 186 shall be deferred in Account 283, Accumulated Deferred Income Taxes - Other or Account 190, Accumulated Deferred Income Taxes, as appropriate, and amortized concurrently with the related expense amount in Account 186.

ERIC A. LEIGHTON, Director,
Office of Accounting and
Utility Finance

Issued:

May 30, 1975

TR-8

(G)

Technical Release Number 10
(Effective Immediately)
Class A and B Utilities

Question:

What accounting procedures should a gas utility implement if the Commission has authorized the company to add a gas "Revenue Stabilization Clause" to its tariff?

Answer

On the effective date of the authorized "Revenue Stabilization Clause" the gas utility should establish:

1. Separate subdivisions of Account 253, Other Deferred Credits, to be entitled, "Revenue Stabilization Amounts - Deferred" and "Interest on Revenue Stabilization Amounts - Deferred";
2. Temporary revenue Account 486, Stabilization Clause Revenues - GAC adjustments;
3. A subdivision of income Account 431, Other Interest Expense, entitled "Interest on Revenue Stabilization Amounts";

4. A subdivision of Account 190, Accumulated Deferred Income Taxes, entitled, "Revenue Stabilization Amounts - Income Tax Deferred"; and,

5. Subdivisions of Account 410.1, Provision for Deferred Income Taxes, Utility Operating Income and Account 411.1 - Provision for Deferred Income Taxes - Credit, Utility Operating Income, both entitled, "Revenue Stabilization Amounts".

Beginning with interruptible and firm sales made on and after the effective date of the "Revenue Stabilization Clause" the gas utility should defer in the separate subdivisions of Account 253, Other Deferred Credits, the monthly revenue stabilization amounts charged or credited to temporary revenue Account 486, Stabilization Clause Revenues - GAC adjustments, and the monthly interest on the deferred balance of such amounts, charged to the subdivision of Account 431, Other Interest Expense, all as determined under the company's "Revenue Stabilization Clause" tariff provisions. Such deferrals should be accumulated over the period specified in the "Revenue Stabilization Clause" tariff provisions. Thereafter, the total amounts remaining deferred should be reduced in each month through debits to the separate subdivisions of Account 253, with contra credits to Account 486, in amounts equivalent to the monthly Revenue Stabilization amounts and related interest credited to firm customers through the Gas Adjustment Clause commencing with such credits reflected in the Gas Adjustment Clause in effect for the month specified in the company's "Revenue Stabilization Clause" tariff provisions.

The gas utility should charge the subdivision of Account 190, with the Federal income tax effect, if any, related to the revenue stabilization amounts deferred in Account 253, and should concurrently credit the subdivision of Account 411.1, Provision for Deferred Income Taxes - Credit, Utility Operating Income, to reflect the tax timing differences arising from institution of the "Revenue Stabilization Clause". The tax effect deferred in the subdivision of Account 190, should be reduced by charges to the subdivision of Account 410.1 Provision for Deferred Income Taxes, Utility Operating Income, in amounts equal to the tax effect of the previously deferred revenue stabilization amounts reflected in the current Gas Adjustment Clause.

ERIC A. LEIGHTON, Director
Office of Accounting &
Utility Finance

Issued:

November 25, 1976

TR-10

(E)

TECHNICAL RELEASE NUMBER 16
(Effective Immediately)
Class A and B Electric Utilities

APPROVED BY THE COMMISSION FEB 6 1980

Question:

In Opinion 78-3, issued March 6, 1978, the Commission approved accounting procedures for research and development (R&D) expenditures, proposed by staff in Case 27154 - Long Range Electric Plans. Since R&D expenditures for any given year may exceed or fall short of the amount of revenues an electric utility is allowed in rates to be used for R&D purposes for that year, the Commission approved deferral accounting to provide for tracking of such shortfalls or overspending. The objective of the deferral accounting is to assure utilities of reimbursement for all R&D expenditures as closely as possible and to prevent an overcollection of revenues from ratepayers for the same purpose. At the same time this accounting shall leave periodic income unaffected by fluctuating R&D activity. What accounting is required to achieve this?

Answer:

Amounts allowed in rates for R&D revenues1/ determined under a kilowatthour (Kwh) sales formula2/ should be credited to the appropriate revenue account. The allowed R&D revenues should

1/ Current month Kwh's billed to ultimate consumers multiplied by a factor (explained in footnote number 2) for the R&D allowance.

2/ Annual R&D costs allowed by the Commission in the accounting utilities' latest rate case divided by the Commission's estimate of Kwh's to be sold in the first year of new rates.

then be charged to Account 456, Other Electric Revenues and credited to a subaccount of Account 188, Investment in Research and Development. As R&D expenses are incurred they should be charged to the subaccount of Account 188 and subsequently distributed to the appropriate expense accounts.

Expenditures for R&D, charged to expense, should be credited to a separate subaccount of Account 930, Miscellaneous General Expense, and charged to the subaccount of Account 188.

On a monthly basis, expenditures for R&D and R&D revenues should be properly matched. To achieve this, the subaccount of Account 456 should be credited and the subaccount of Account 930 should be debited, with an amount representing the actual expenditures for R&D not in excess of R&D revenues billed, plus any credit balance in the subaccount of Account 188, representing revenues deferred in prior months.

A credit balance in the subaccount of Account 188 would indicate that expenditures for R&D fell short of the amount of revenues the utility was allowed in rates for R&D purposes. The related Federal income tax effect, deferred as a credit in Account 411.1, Provision for Deferred Income Taxes - Credit, Utility Operating Income, should be debited to Account 190, Accumulated Deferred Income Taxes; as the deferred revenues are offset by future R&D expenses, the amounts in Account 190 should be charged to income.

A debit balance in the subaccount of Account 188 would indicate that expenditures for R&D exceeded the amount of revenues the utility was allowed in rates for R&D purposes. The related Federal income tax effect, deferred as a debit in Account 410.1, Provision for Deferred Income Taxes, Utility Operating Income, should be credited to Account 283, Accumulated Deferred Income Taxes - Other; as the deferred expenses are offset by future R&D revenues, the amounts in Account 283 should be credited to income.

The accounting described above is necessary to fulfill the Commission's intent, as expressed in Opinion 78-3, to apply only to such R&D expenditures that are treated for accounting purposes as current expenses, and to provide for tracking by matching amounts of revenue allowed in rates for R&D with expenditures for R&D activities.

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