STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held in the City of Albany on December 14, 2017

COMMISSIONERS PRESENT:

John B. Rhodes, Chair
Gregg C. Sayre
Diane X. Burman
James S. Alesi

CASE 17-M-0363 - In the Matter of Accounting and Ratemaking Related to the Financial Accounting Standards Board's March 2017 Accounting Standards Update entitled Compensation-Post Retirement Benefits (Topic 715)

ORDER CONCERNING THE ACCOUNTING AND RATEMAKING TREATMENT FOR PENSIONS AND POST RETIREMENT BENEFITS OTHER THAN PENSIONS

(Issued and Effective December 18, 2017)

BY THE COMMISSION:

INTRODUCTION

The Financial Accounting Standard Board (FASB) issued an Accounting Standard Update for Compensation – Retirement Benefits (Update) in March 2017. The Update changes the accounting and reporting required to be used by companies, including those regulated by the Commission, for pension and other post-retirement benefit (OPEB) costs under Generally Accepted Accounting Principles (GAAP). The implementation date is as early as the fiscal period beginning after December 15, 2017 for public business entities.[1] The stated purpose of the

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[1] FASB Accounting Standard Update (ASU 2013-12) defines a public business entity.

Update is to improve the presentation of net periodic pension and OPEB costs to provide more transparency to financial statement users.

The main provisions in the Update include a change in presentation of the net periodic pension/OPEB costs in employers' financial statements. Currently, under GAAP, all components of net periodic pension/OPEB costs, including:

1) service cost;
2) interest cost;
3) return on plan assets;
4) gains/losses;
5) prior service cost;
6) transition asset/obligation; and,
7) gains/losses on settlement or curtailment

are presented in the income statement as an operating expense, and therefore, included as part of operating income. Under the requirements of the Update, only the service cost component of the net periodic pension/OPEB cost will continue to be included in operating income as an operating expense. The other six components would now be required to be presented separately from the service cost component, as a part of other income and expenses and below the subtotal of income from operations. Since these cost elements are primarily driven by market forces and variances from actuarial assumptions, as opposed to company operations, and are not predictive, financial statement users preferred that they be reported separately from operating income to improve operations transparency.

A second major ramification of the Update is a change in the accounting related to the capitalization of pension/OPEB costs. Prior to the Update, utilities were allowed to capitalize a portion of all seven components of the net periodic pension/OPEB costs, when applicable based on labor capitalization rates.[2] The Update will only allow capitalization of the service cost component of the net periodic pension/OPEB costs since GAAP do not allow non-operating costs to be capitalized. This shift of non-service components of pension/OPEB costs from capital to expense will result in a change in the timing of cost recovery in rates as these costs will no longer be capitalized and recovered over the book life of the related plant, but rather be expensed as incurred. The net impact of the six cost components may be positive or negative in any given year, so the change in accounting will not necessarily be an immediate driver of rates. The accounting change will however increase volatility in pension/OPEB expenses. The ultimate amount customers pay for these costs does not change under either accounting methodology, it is just the timing of the recovery that will change.

PUBLIC NOTICE AND COMMENTS

On June 23, 2017, the Secretary issued a Notice Soliciting Comments Regarding Accounting Standards Update for Compensation – Retirement Benefits (Notice). Pursuant to the State Administrative Procedure Act (SAPA) §202(1), a Notice of Proposed Rulemaking was published in the State Register on June 27, 2017 (17-M-0363SP1). The Notice included twelve specific issues to be addressed in the Comments that related to the potential impact of this FASB Update on revenue requirement, the Uniform System of Accounts, Annual Reports, and the Commission’s Statement of Policy and Order Concerning the

[2] Labor costs associated with Construction Work in Progress (CWIP), are generally capitalized and included in the plant balances. Prior to the Update, all of pension and OPEB costs were also capitalized as a labor overhead and were included as part of the plant balances.

Accounting and Ratemaking Treatment for Pensions and Post-Retirement Benefits Other Than Pensions issued in Case 91-M-0890 on September 7, 1993 (Policy Statement).

The following utilities submitted comments:

Consolidated Edison Company of New York, Inc. (Con Edison)
Orange and Rockland Utilities, Inc. (O&R)
Niagara Mohawk Power Corporation d/b/a National Grid(Grid)
KeySpan Gas East Corporation d/b/a National Grid (KEDLI)
The Brooklyn Union Gas Company d/b/a National Grid (KEDNY)
Central Hudson Gas and Electric (CHGE)
National Fuel Gas Distribution Corporation (NFG)
Verizon New York Inc. (Verizon)
New York American Water Company, Inc. (NYAW)

All the commenting utilities, except for NYAW, support the Commission's adoption of the Update for regulatory accounting and rate making purposes. NYAW alleges greater volatility to customer rates as a reason not to adopt the Update and prefers to continue to account for pensions and OPEBs under the current methodology for ratemaking purposes.

LEGAL AUTHORITY

Pursuant to Public Service Law (PSL) §§ 5, 65(1), and 66 (4) and (12), 80(3) and (10); 89-c (3) and (10); 95 (1) and (2) the Commission has the legal authority to prescribe uniform methods of keeping accounts, records and books. As such, the Commission has the legal authority to review the FASB Accounting Standard Update for Compensation – Retirement Benefits and adopt for regulatory accounting and ratemaking purposes, as prescribed in this Order.

DISCUSSION

The primary argument against adopting the Update is that it will add volatility to customer rates. Whenever revenues or expenses are recognized immediately through the income statement, as opposed to being capitalized and recovered over the life of an asset, it will add volatility to the revenue requirement. The table below reflects estimated near-term rate impacts of adopting the Update for the major utilities, based on the companies' reported revenue requirement impacts and the most recent delivery revenues.

Average Annual Revenue Requirement Impact (% of Delivery Revenues)		
Company	**Avg Impact on Revenue Requirement**	**Years Included in the Average**
Con Edison	-0.23%	(2018-2022)
O&R	0.48%	(2018-2022)
NMPC	-0.25%	(2019-2021)
KEDNY	0.99%	(2017-2019)
KEDLI	0.90%	(2017-2019)
CH	-0.56%	(2018-2022)
NYSEG *	0.13%	(2017)
RGE *	0.83%	(2017)
NYAW **	0.07%	(2017)
SUEZ-NY **	0.15%	(2017)
SUEZ-Westchester **	0.07%	(2017)

* NYEG/RGE data based on responses to information requests, as they did not submit official comments.

** NYAW/Suez data based on responses to information requests. Revenue requirement impacts based on total water revenues.

There are several arguments in favor of adopting the Update and keeping the regulated books in conformance with GAAP accounting. Key arguments include avoiding the complexity, potential errors and costs associated with maintaining separate books. If the GAAP books recognize certain costs immediately through the income statement, and the regulated books allow those same costs to be capitalized as assets on the balance sheet and charged annually to income (depreciation expense) over the life of an asset, complex and long-lasting differences on the two sets of books would result and would not be easily reconciled. It is conceivable, depending on the magnitude and direction of these costs, over time the two sets of books may bear little resemblance to one another, particularly on the balance sheet as it relates to assets and equity. The variances in the two set of books would include plant balances, depreciation expense, accumulated depreciation, pension expense, current income taxes, deferred income taxes, accumulated deferred income taxes, annual net income, retained earnings, and the asset and equity segments of the balance sheet. Reconciling the two sets of books would be very complex and would involve tracking vintage year differences spanning asset-lives that can be greater than 80 years. Anytime complexity of this magnitude is introduced, it increases the potential for errors.

Many of the companies commented that maintaining two sets of books will require costly system changes. If the Update is not adopted for its regulatory books, the utilities would have to track the differences in fixed assets, and all the other accounts that will be impacted. The companies would incur upfront costs to purchase or develop software systems for dual tracking functionality and would incur incremental costs for ongoing operating and maintenance of the systems. In addition, Commission adoption of the Update will avoid the increased costs for an audit opinion obtained from outside auditors for each set of books, due to additional procedures to audit the differences in the regulatory set of books.

After a careful review of all comments submitted in response to the Notice, we are adopting the Update for regulatory accounting and ratemaking purposes. Although the added volatility to rates concerns us, it is important to recognize that over the long-term customers will pay the same amount for these costs under either accounting methodology. We prefer to keep the regulated books in-line with GAAP books, absent compelling reasons to deviate, as it reduces complexity, it is a recognized standard that financial statement users are familiar with, it is a common standard that allows like comparisons to other entities that maintain GAAP books, and avoids the costs associated with maintaining two sets of books. Adoption of the Update is in the public interest.

Accounting, Reporting and Ratemaking

The non-service cost components are largely affected by market returns and actuarial assumptions, rather than results from operations, which was the primary reason why this Update moved these elements from the operating income to other income and deductions section of the income statement. Other income and deductions section of the income statement is often referred to as “below-the-line”.

For ratemaking purposes, non-service cost elements of pension/OPEBs costs have always been, and continue to be, legitimate and recoverable costs of doing business for utilities. We will continue to require the utilities to book these cost elements in the same accounts[3] that they have been using, which are above-the-line for Commission reporting and ratemaking purposes. This approach keeps the income from

[3] USOA Account *926-Employee Pensions and Benefits* for water, electric and gas companies, and USOA Account *6728 -Other General and Administrative* for telecommunications companies.

operations on the income statement consistent with its ratemaking treatment.

This difference of above-the-line treatment for regulatory books and below-the-line treatment for GAAP books is presentational in nature and only relates to where these costs appear on the income statement, and does not impact the underlying accounting.

Regulatory accounting for pension/OPEBs costs will remain transparent to users of the Annual Reports filed with the Commission. Cost component details will continue to be reported in the Pension and OPEB schedules in the Commission Annual Report. Any differences between Commission and GAAP books will continue be reported on the "Reconciliation Between PSC and Stockholders Annual Report" schedule.

CONCLUSION

After all considerations discussed above, we adopt the FASB Update for Compensation – Retirement benefits (Topic 715), as it relates to not capitalizing non-service components of pension/OPEB costs. For ratemaking and Commission accounting and reporting purposes, non-service costs will continue to be accounted for above-the-line as part of operating income. The companies should implement the Update for regulatory accounting and reporting purposes coincident with their adoption of the Update for GAAP reporting purposes.

The Commission orders:

1. All companies or entities regulated by the Commission that have defined-benefit pension plans and/or post-employment benefits (listed in Appendix A) are to adopt the FASB Topic 715 Update as it relates to not capitalizing non-service components of pension/OPEB costs. The date of adoption should

be concurrent with the adoption of the Update on their GAAP books.

2. For ratemaking and Commission accounting and reporting purposes, such companies and entities shall continue to use the same USOA accounts that they have traditionally used to account for non-service cost components of pension/OPEB net periodic costs.

3. The Secretary, in her sole discretion, is authorized to extend the deadlines set forth in this Order provided the request for such extension is in writing, including a justification for the extension, and filed on a timely basis, which should be on at least one day's notice prior to the affected deadline.

4. This proceeding is continued.

By the Commission,

(SIGNED) KATHLEEN H. BURGESS
Secretary

This order applies to the following utility companies, if they have a defined benefit pension and/or OPEB plan:

<u>Telephone Companies:</u>

1 Alteva of Warwick, LLC

2 Armstrong Telephone Company Armstrong Telecommunications

3 Berkshire Telephone Corporation D/B/A Fairpoint Long Distance

4 Cassadaga Tel. Corp., Dunkirk & Fredonia Tel. Co.

5 Champlain Telephone Company

6 Chautauqua and Erie Telephone Corporation, D/B/A Fairpoint Communications

7 Chazy & Westport Telephone Corporation

8 Citizens Telephone Company of Hammond, New York, Inc.

9 Crown Point Telephone Corp.

10 Delhi Telephone Company

11 Deposit Telephone Company, Inc. / Tds Telecom

12 Edwards Telephone Company, Inc. / Tds Telecom

13 Empire Telephone Corp.

14 Fishers Island Telephone Corp.

15 Frontier Communications

16 Germantown Telephone Co., Inc., D/B/A Gtel Teleconnections

17 Hancock Telephone Corporation

18 Margaretville Telephone Company, Inc.

19 Newport Telephone Company

20 Nicholville Telephone Company, Inc.

21 Norlight Telecommunications, Windstream New York

22 Oneida County Rural Telephone Company

23 Oriskany Falls Telephone Corp.

24 Pattersonville Telephone Company

25 Port Byron Telephone Company

26 SLIC Network Solutions, Inc.

27 State Telephone Company, State Telephone Long Distance Company

28 Taconic Telephone Corp. D/B/A Fairpoint Communications, Taconic Telcom Corp.

29 The Middleburgh Telephone Company

30 Township Telephone Company, Inc.

31 Trumansburg Tel. Co., Inc., Finger Lakes Tech. Group, Inc., Ontario Tel. Co., Inc., Finger Lakes Comm. Group Inc.

32 Verizon New York Inc.

33 Vernon Telephone Company

Electric/Gas/Steam Companies:

34 Central Hudson Gas & Electric Corporation

35 Chautauqua Energy Management, Inc.

36 Chautauqua Utilities Inc.

37 Consolidated Edison Company of New York, Inc.

38 Corning Natural Gas Corporation

39 Fillmore Gas Company, Inc.

40 Fishers Island Electric Corporation

41 GPU Service

42 KeySpan Gas East Corporation d/b/a National Grid

43 N.E.A. Cross of N.Y. Inc.

44 National Fuel Gas Distribution Corporation

45 New York State Electric & Gas Corporation

46 Niagara Mohawk Power Corporation d/b/a National Grid

47 Orange and Rockland Utilities, Inc.

48 Reserve Gas Company Inc.

49 Rochester Gas & Electric Corporation

51 St. Lawrence Gas Company, Inc.

52 The Brooklyn Union Gas Company d/b/a National Grid NY

53 Valley Energy, Inc.

Water Companies:

54 Fishers Island Water Works Corp

55 Heritage Hills Water Works

56 New York American Water Co.

57 Saratoga Water Services, Inc.

58 Suez Water New York Inc.

59 Suez Water Owego-Nichols Inc.

60 Suez Water Westchester, Inc.