

# Roundtable Discussion: Accounting and Ratemaking

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# Overview

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- Fuel Clause
- Determining the Rate of Return
- Uniform System of Accounts and Reporting
- Policies for Information Disclosure and Confidentiality Issues



# Fuel Clause

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# Generation Revenue Requirements

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- Base rates
  - Net generation plant \$1.7 billion
  - Return on net generation plant ~ \$125 million
  - \$181 million expenses for operations and maintenance
- Adjustment clauses
  - ECA
    - \$500 million fuel
    - \$676 million purchased energy
  - PCCA: \$390 million
  - DSMCA: \$50 million
  - Renewables Surcharge: \$50 million



# Reconciliation to Actual Costs

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- Base rate revenues generally not reconciled with actual costs incurred
- Adjustment clauses generally fully reconcilable with actual costs incurred
  - Riders set at levels to recover current levels of costs
  - Based on projections made before rate takes effect



# Initial ECA

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- Recovered fuel costs
  - Coal for utility-owned plants
  - Natural gas for utility-owned and IPP plants
- Purchased energy
  - From IPPs with long-term PPAs
  - From others with short-term economic energy purchases
- Uniform \$/kWh charge for all customers
- Changed annually
- Interim changes if over or under recoveries of \$40 million or more



# Current ECA

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- Recovers fuel costs and purchased energy as previous ECA
- Recovers portion of the total costs of renewables (equivalent to the cost of avoided fossil fuel resources)
- Incentives to the utility
  - Baseload incentive to maximize use of coal plants
  - Economic energy purchase incentive
- Uniform \$/kWh charge for all customers
- Changes each quarter (every three months)



# Proposed ECA

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- Similar to current ECA in terms of types of costs and incentives recovered
- Class specific ECA charges
  - Residential customers would pay different fuel charge than non-residential and industrial customers
- Largest customers would pay time-of-use (TOU) ECA
- Every charge would change monthly





# Determining the Rate of Return

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# Rate of Return

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- Represents the amount allowed to be earned, expressed as a percentage of the utility's rate base
- The rate of return (ROR) is intended to allow the utility to:
  - Meet its obligations to present investors (interest and dividends)
  - Compete on reasonable terms in the financial markets for future capital requirements
  - Primarily consists of debt, preferred stock and common equity
- Often the most controversial component of the revenue requirement



# Cost of Equity

- Corresponds to the return on equity (ROE) established in Phase I
- Methods for determining the cost of equity are largely immaterial so long as the outcome is reasonable to both consumers (rate impacts) and investors (return on equity)
- ROE is generally calculated by dividing the Company's earnings by total shareholder equity
- Commonly used models to estimate the cost of equity include:
  - Discounted cash flow (DCF)
  - Capital asset pricing (CAPM)
  - Risk premium (RP)
  - Comparable earnings (CE)



# Example Capital Structure

	<u>Amount</u>	<u>Ratio</u>		<u>Cost</u>		<u>Composite Return</u>
Debt	\$80	40%	x	8.0%	=	3.2%
					+	
Equity	<u>\$120</u>	60%	x	12.0%	=	<u>7.2%</u>
Total	\$200					<b>10.4%</b>

ROE

ROR




# Uniform System of Accounts

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# Uniform System of Accounts

- Cost-reporting protocols
- Specific accounting rules for reporting capital expenditures and operating costs
  - Capital asset valuation
  - Depreciation schedules
  - Taxes
  - Ongoing operating cost categories (cost of sales, salaries, benefits, incentives)
  - Allocation of costs between lines of business (regulated and unregulated)
  - Financial instruments (think Enron)

THIS FILING IS	
Item 1: <input type="checkbox"/> An Initial (Original) Submission OR <input type="checkbox"/> Resubmission No. _____	
Form 1 Approved OMB No. 1902-0021 (Expires 12/31/2011) Form 1-F Approved OMB No. 1902-0029 (Expires 12/31/2011) Form 3-Q Approved OMB No. 1902-0205 (Expires 1/31/2012)	
	
<b>FERC FINANCIAL REPORT</b> <b>FERC FORM NO. 1: Annual Report of</b> <b>Major Electric Utilities, Licensees</b> <b>and Others and Supplemental</b> <b>Form 3-Q: Quarterly Financial Report</b>	
<small>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 a confidential nature.</small>	
Exact Legal Name of the Respondent (Company)	Year/Period of Report End of <u>2008.Q4</u>
FERC FORM No. 1/3-Q (REV 02-04)	



# The FERC Form 1

- Three-digit whole number system by cost category
- Consistent, year-to-year record keeping
- Accounts create income statements and balance sheets
- Accounts feed into ratemaking "models"

100-199	Assets and other debits
200-299	Liabilities and other credits
300-399	Plant accounts
400-432; 434-435	Income accounts
433; 436-439	Retained earnings accounts
440-459	Revenue accounts
500-599	Production, Transmission, and Distribution accounts
900-949	Customer, Customer Service and Information, Sales, and Administrative and General Expenses



# Information Sharing

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# Information Gathering Powers

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- Reporting requirements
  - Annual financial reports (SEC 10-Ks, FERC Form 1s)
  - Production reports (system supply)
  - Service quality reports (outages, complaints, metering)
  - Miscellaneous reports (RESA budget, street lighting)
- Audit and inspection
  - Books, records, assets
  - Verification and litigation
- Subpoenas
  - Enforceable by courts
- Voluntary
  - Just ask!



# Rate Proceeding Discovery

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- Parties pose questions and request data from the utility through their attorneys in order to prepare filing into the record that are responsive to the utility's requested change in rates
- Utility obligated to respond to questions and data requests within a specified amount of time as long as the requests are relevant and reasonable
- Utility may object to requests
- Disputes concerning discovery settled by the Commission or by an Administrative Law Judge



# Confidentiality

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- Commission protects confidential information
  - Formal rules and procedures for handling confidential material
  - Practices for not compromising confidential material
    - Hard copies
    - No email of electronic files
- Staff signs a non-disclosure agreement each year
  - Covers all proceedings
  - Certain extraordinary cases require Staff to commit to limited use and access
- Other parties must sign case-specific non-disclosure agreements

