Roundtable Discussion: Accounting and Ratemaking

Ron Davis

Principal Economist

Colorado Department of Regulatory Agencies

Public Utilities Commission 1560 Broadway, Suite 250 Denver, CO 80202

P 303.894.2883 | F 303.869.0333

Email: ronald.davis@dora.state.co.us







Overview

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





Fuel Clause

Generation Revenue Requirements

- 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
 - o \$500 million fuel
 - o \$676 million purchased energy
 - PCCA: \$390 million
 - DSMCA: \$50 million
 - Renewables Surcharge: \$50 million





Reconciliation to Actual Costs

- 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

- 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

- 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

- 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

Rate of Return

- 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>	Composite <u>Return</u>
Debt	\$80	40%	x 8.0%	3.2%
Equity	<u>\$120</u>	60%	x 12.0% =	<u>7.2%</u>
Total	\$200		ROE	10.4%



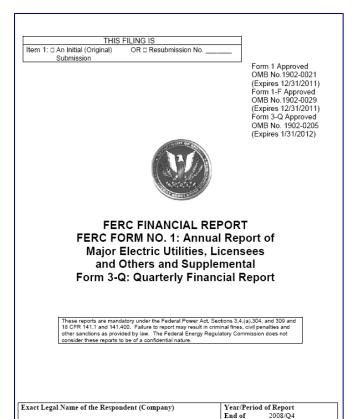


Uniform System of Accounts

Uniform System of Accounts

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

- 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)







The FERC Form 1

- Three-digit whole number system by cost category
- Consistent, yearto-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

Information Gathering Powers

- 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

- 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

- Commission protects confidential information
 - Formal rules and procedures for handling confidential material
 - Practices for not compromising confidential material
 - o Hard copies
 - o 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 nondisclosure agreements



