Capitalization Policy and Capital Decisions

Spring EEI Conference 2018  San Diego, CA
Course Objectives

- Capital Policy Development and Update Process
  - Development/ level of details
  - Frequency and drivers of updates

- SOX Controls
  - Ownership of capital decisions
  - Standard vs. Non-Standard

- Capital Decisions
  - Form Examples – tangible & software
  - Routing
Overview and History

- The initial development of Duke’s Capitalization Policy was an evolution from G/L account descriptions to an official policy to address broad topics and provide guidance.
- Duke has merged with Cinergy, Progress Energy, and Piedmont Natural Gas.
  - Each integration has enhanced the Policy by finding best practices between entities.
- Updates are made annually, with implementation 1/1 of following year
  - Mid-year updates are handled via memo and direct communication
Layout and Structure of the Policy

- Table of Contents
- Integration Matrix (used for mergers)
- Capitalization Concepts
  - The economics of capitalization
- Regulatory & Accounting Guidance
  - FERC and GAAP Overview
- Capitalization Guidelines
  - Basics of FERC and GAAP capitalization
  - Includes construction matrix “at a glance”
- Special Topics
  - Ranges from Project Approvals to Plant Retirements (and everything in between!)
## Drivers of updates

- Recent Capital Decisions (only if significant)
- New processes affecting capital projects (examples: Agile development)
- New Accounting Standards (examples: Cloud, Pension, Lease)
- Clarification of existing guidelines
- Mergers
Merger Integration Process

- Legacy employees from each Asset department meet over several sessions to discuss each section of the Policy.
- Differences in practice and application are quantified and escalated for discussion with management.
- Example:
Summary of the changes are provided to all legacy Policy users, and a matrix is included in the Capital Policy for 1-2 years.

Example:

<table>
<thead>
<tr>
<th>Issue</th>
<th>Duke Energy</th>
<th>Piedmont Natural Gas</th>
<th>Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Facility Renovations &amp; Leasehold Improvements</td>
<td>Leasehold improvement policy applies to both owned facilities and facilities that are being accounted for as operating leases or capital leases.</td>
<td>Same</td>
<td>Leasehold improvement policy applies to both owned facilities and facilities that are being accounted for as operating leases or capital leases.</td>
</tr>
</tbody>
</table>

The entire Duke/PNG Summary section of the Policy is 15 pages long.
SOX Controls
Finance groups have accountability for capital determinations

Concept of “Standard” and “Non-Standard” project type will drive project approvals

**Standard Definition:**
- Complete install or removal of an entire Unit of Property defined in our Catalog
- Costs are capital per Policy

**Non-Standard Definition:**
- New Capital spares
- Sales or Purchases of Assets
- Capital Rebuilds
- Plant License extensions or modifications
- Preliminary study & investigation (183)
- Research and Development
- Software
- Substantial betterments & minor item additions
- Training
Completion of the Capital Decision Form
• Provides Support for Auditors and Commissions
• Drives Consistency
• Enhances Learning
• Efficient
Enter the basic details about your project
Select the appropriate request type, status, date submitted, and business function that pertains to your request.
Clicking in one of the fields will reveal a drop down menu with various options.

<table>
<thead>
<tr>
<th>Request Type:</th>
<th>Choose an item.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Status:</td>
<td>Choose an item.</td>
</tr>
<tr>
<td>Date Submitted to Asset Acctg</td>
<td>Click here to enter a date.</td>
</tr>
<tr>
<td>Date Completed by Asset Acctg</td>
<td>Click here to enter a date.</td>
</tr>
<tr>
<td>Requestor Name:</td>
<td></td>
</tr>
<tr>
<td>Applies to Business Function:</td>
<td>Choose an item.</td>
</tr>
<tr>
<td>Finance Approver:</td>
<td></td>
</tr>
<tr>
<td>Asset Responder:</td>
<td></td>
</tr>
<tr>
<td>Asset Approver:</td>
<td></td>
</tr>
<tr>
<td>Asset Director:</td>
<td></td>
</tr>
<tr>
<td>Subject:</td>
<td></td>
</tr>
</tbody>
</table>
Based upon the selection of Request Type, fill out the appropriate sections listed in the Index below (details of each request type are explained in the following slides):

<table>
<thead>
<tr>
<th>Index to Form: The following sections must be completed as it pertains to your request.</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Unit of Property Requests</td>
</tr>
<tr>
<td>Substantial Betterment</td>
</tr>
<tr>
<td>Substantial Addition</td>
</tr>
<tr>
<td>Overhauls, Rebuilds, Refurbishments</td>
</tr>
<tr>
<td>183 Study Projects</td>
</tr>
<tr>
<td>Other Questions</td>
</tr>
<tr>
<td>Project Suspension</td>
</tr>
<tr>
<td>Project Un-Suspend (Reopen for charging)</td>
</tr>
</tbody>
</table>

**ONLY the pertinent sections need to be completed based on the type of request.**
Section 1: Explain the question or issue and give basic information

<table>
<thead>
<tr>
<th>#</th>
<th>Question</th>
<th>Response</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1</td>
<td><strong>Capitalization Question or Item:</strong> Enter the capitalization question in this area. This MUST be completed for this request to proceed.</td>
<td></td>
</tr>
<tr>
<td>1.2</td>
<td>Which section of the Capitalization Policy is most relevant to this request?</td>
<td></td>
</tr>
<tr>
<td>1.3</td>
<td>Is this currently budgeted as Capital or O&amp;M?</td>
<td></td>
</tr>
<tr>
<td>1.4</td>
<td>Was this previously accounted for as O&amp;M?</td>
<td></td>
</tr>
<tr>
<td>1.5</td>
<td>Please provide the current Project ID if available.</td>
<td></td>
</tr>
</tbody>
</table>
➢ **Fill out other pertinent sections**

### Section 6: 183 Study Projects

| 6.1 | Provide the scope of the project. |
| 6.2 | What options are being considered? |
| 6.3 | What is the UoP that may eventually be installed? |
| 6.4 | Define the common costs between the different options being studied. |
| 6.5 | What plan is being laid out to track costs between the different options as well as costs shared? |
| 6.6 | What is the process for reviewing the study work and deadline for the decision to be made to either move or not move forward? |
Asset Accounting provides the relevant guidance related to the decision along with discussion points.

Final Conclusion is provided.

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**Asset Accounting Response:**

From Duke Energy 2018 Capitalization Guidelines:

Preliminary studies, plans, and investigations, ("183") for the purpose of determining the feasibility of utility projects should be charged to the appropriate Preliminary Survey and Investigation account. If construction results, the Preliminary Survey and Investigation account should be credited for the study costs directly attributable to the new plant construction and charged to the appropriate plant account (e.g., 107, Construction Work in Progress). Study costs not directly attributable to the new construction should be credited to the Preliminary Survey and Investigation account and charged to the appropriate operating expense account. Note that common costs which are incurred regardless of the option chosen shall be allocated equally to each of the options (i.e., if 4 options exist and one common project, each option will receive an allocation of 25% of the common project).

Preliminary Study and Investigation Accounts

P. 183 – Preliminary survey and investigation – Electric – This account shall be charged with all expenditures for preliminary surveys, plans, investigations, etc., made for the purpose of determining the feasibility of electric utility projects under contemplation and costs of studies and analyses mandated by regulatory bodies related to plant in service.

Further clarification was provided to AARG that the purpose of the project is to study the feasibility between building a site. Although only one site is being considered, two options for the site are being considered. Construction will result from either option chosen. The purpose of studying the cost associated for each option of the ongoing O&M that include: per diem, hotels, airfare, mileage, catering, planned attrition of trainers, and the planned throughput of the trainees for both I&D line workers and the supporting engineers, meet the criteria for being directly attributable to the new construction.

**Conclusion:**

AARG agrees that the above activities qualify as a Capital Study Project. Time spent evaluating each option shall be allocated proportionately. If a proportionate allocation of cost is not prudently identifiable, those costs shall be split between the options evenly, with the costs of the option not chosen charged to O&M.
Software Request Form
The Software Request Form is built in Excel. Macro functionality helps drive the correct information up front.
Answering “Yes” to specific questions on the Questionnaire triggers an expected amount on the cost template.

11. Will you have data conversion activities?

Yes
New Functionality must be explained in detail

### Upgrade/Enhancement to Existing Duke-Owned Software

**New Functionality**

*Instructions:* Per the capital policy, in order for upgrades and enhancements to be capitalized, they must result in significant new functionality. Additional functionality is defined as modifications to software to enable it to perform tasks that it was previously incapable of performing.

In the boxes below, please describe each item of additional functionality and the benefit that it provides; further, expand on how the software performs current state versus future state.

<table>
<thead>
<tr>
<th>New Functionality/Benefit Provided</th>
<th>Current State - What is the current process?</th>
<th>Future State - What will the future process be?</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Submittal of the Capital Decision Form
Uploading a Capital Decision Request to the AARG SharePoint Page

Navigate to: https://team.duke-energy.com/sites/CPQ/SitePages/Home.aspx
You will be prompted to give your Capital Decision Request a name and select the project type from the drop down. Selecting the project type and clicking Check In will route your request to the appropriate AARG team member and send a confirmation email.
Capital Decisions

- Routing – SharePoint Nintex Workflow

- All decisions reside in a “Pending” folder where the status is tracked. Our business partners can see this folder.
Capital Decisions
  ▪ Routing – SharePoint Nintex Workflow

Decisions that need follow up from business partners have a separate folder:
Capital Decisions

- As each decision progresses, email notifications are sent to the requester and the Asset analyst.

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**DISTRIBUTION Capital Decision Request**

- *Nintex*
- This message was sent with High importance.

**Sent:** Wed 4/18/2018 10:20 AM  
**To:** Durham, Kristi M.  
**Cc:** Miller, Linda

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**Workflow Notification**

A new distribution capital decision request has been uploaded to the SharePoint Site.

[https://team.duke-energy.com/sites/CPQ/Pending%20Capital%20Decisions/Forms/AllItems.aspx](https://team.duke-energy.com/sites/CPQ/Pending%20Capital%20Decisions/Forms/AllItems.aspx)
Final decisions are archived to libraries by functional area.