Ratemaking Trends and Industry Accounting

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On the Regulatory Front

- Politics and the Influence of the Legislature
  - Political landscape
    - Governorship and legislative chambers
  - Clean energy platforms/Electric vehicles
  - Nuclear subsidies
  - Pipeline integrity and natural gas

- Rate case activity
  - During 2018, 140 rate cases completed
  - As of March 8, 62 pending rate cases (E-36; G-26)
  - 70+ rate freezes in effect
  - Trends in authorized returns on equity
  - Issues related to non-rate case proceedings
  - RRA view—less investor risk where commissioners appointed versus elected
Where Are We Going?

- Performance and incentive-based ratemaking
- Alternative regulatory structures
- Affordability
- Green New Deal—AOC
- Mergers and Acquisitions
- Tax reform—yes, still
- ESG
  - Industry efforts
  - Shareholder proposals
  - Rating agencies
- The FERC and Commission complement
Industry accounting
Scenario 1

- Utility company A is acquiring utility company B
- In conjunction with the merger agreement, utility company A will provide merger bill credits to over the next three years with a monthly bill credit
- The respective state commission and FERC approvals for the merger occurs on November 20
- The merger subsequently closes on November 27

**Question:** In the utility company A’s 2018 10-K, what are the accounting and disclosure implications of these credits?
Scenario 2

- A utility holding company owns two entities, a regulated utility and a merchant generation business.
- The utility holding company is moving a 150 MW solar facility from its merchant generation business to the regulated utility.
- The carrying value of the solar facility is $125 million on the merchant generator’s books and its remaining useful life is 25 years.
- The company has filed its testimony requesting a transfer of the plant at book value.
- Intervenors have filed testimony objecting to transferring the plant at book value.
- The company expects the commission will allow the transfer, but limit the recovery to fair market value.
- The commission is expected to issue an order after the financial statements are issued.
- Fair market value at the balance sheet date is estimated at $100 million.

**Question:** What are the accounting implications of this proposed transfer of the plant from the merchant to the regulated utility?
Scenario 3

- A major storm in September 2018 causes extensive damage to the company’s distribution system
- The company has insurance coverage of $100M per event after a $10M deductible
- The estimated cost to restore the system is: $40M in repairs expense and $80M in capital expenditures (replacement)
- The assets damaged in the storm were primarily older assets with immaterial remaining book values
- The repair costs and capital expenditures had all been incurred as of December 31
- The insurer has acknowledged that the event is covered by the policy
- On December 12, the insurer notifies the company that it will pay a partial payment of $24M on January 5
- Total amount of insurance recovery is uncertain – insurer is expected to challenge if some of the facilities could have been replaced

Company analysis of likely ultimate insurance recovery:

- Total damages 120
- Less deductible (10)
- Not allowed (14)
- Probable recovery 96

**Question:** Should the company record a receivable from the insurance company at December 31? If so, how much?
Scenario 4

- A gas company has currently ramped up its gas pipeline reliability initiatives and began spending $XX million per year associated with this program and recorded a regulatory asset for the incremental costs that these costs were probable of recovery.
- As part of the current rate case, the commission has approved recovery of the incremental costs of 2018 associated with these initiatives.
- The company anticipates maintaining this level of spending in 2019 and in future years.
- The commission did not allow for the recovery of the future costs associated with the gas pipeline. The test year level for these expenses were included at prior spending levels.

**Question:** What are the accounting and disclosure implications of the commission’s decision?
Scenario 5

- Utility company A has a 50% interest in a joint venture that is accounted for as an equity method.
- As a result of declining sales and other business challenges at the joint venture, the estimated value of the joint venture is approximately 30% below the carrying amount.

**Question:** Is there a need to evaluate this investment for impairment? If so, how should that be done?
Scenario 6

• As a result of the December 2017 tax legislation, Utility Company remeasured its deferred income tax asset from a federal rate of 21% as of December 31, 2017.

• As the Company anticipated its regulator would require future rate reductions for the “excess deferred income taxes” related to its rate regulated operations, the Company reflected the expected future revenue requirement in its liability account at the end of 2017.

• On March 28, 2018, the commission staff initiated a proceeding for all companies in the state, providing that the lower federal tax rates be tracked effective January 1, 2018, with the amount tracked to be included in the next base rate case.

• The commission issued an order in May 2018 approving the tracking mechanism for accounting for deferred income taxes.

• The company expects to file its next base rate case in March 2019 for rates effective January 1, 2020.

• The company and its regulatory counsel believe that the commission has no statutory authority to look back to January 1, 2018; therefore, the company should be able to “keep” the benefits of the lower three-month period from January 1 to March 15.

Questions: Should the company reflect a regulatory liability for the 35% vs. 21% rate differential in 2018? Should the company begin amortization of the excess deferred income tax regulatory liability in 2018? When should amortization commence January 1? March 28? When new rates are in effect 1-1-20?
Scenario 7

- On a calendar year basis, actual utility revenues are compared against what revenues would have been under typical weather.
- Utility A must make a filing by May 1 of the following year (May 1, 2019) with the adjustment and the adjustment order.
- Commission must issue an order by December 1, 2019.
- Customer bills are adjusted the subsequent year (2020 is the first year) to collect the additional revenues due to overcollection.
- At September 30, 2018, calculations show that revenue has been overcollected year to date by $25 million.
- At December 31, 2018, calculations show that revenue has been undercollected by $25 million.

**Question:** What accounting entries, if any, does A make at September 30, 2018 and December 31, 2018 on an annual basis in the accounting literature?
Questions?
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