

State of Florida



## Public Service Commission

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### -M-E-M-O-R-A-N-D-U-M-

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**DATE:** November 21, 2006

**TO:** Director, Division of the Commission Clerk & Administrative Services (Bayó)

**FROM:** Division of Economic Regulation (Slemkewicz, Kyle)  
Office of the General Counsel (M. Brown)

**RE:** Docket No. 060733-EI – Petition for authority to use deferral accounting for creation of a regulatory asset or regulatory liability to record charges or credits that would have otherwise been recorded in equity pursuant to balance sheet treatment required by Statement of Financial Accounting Standards (SFAS) No. 158, by Tampa Electric Company.

**AGENDA:** 12/05/06 – Regular Agenda – Proposed Agency Action – Interested Persons May Participate

**COMMISSIONERS ASSIGNED:** All Commissioners

**PREHEARING OFFICER:** Administrative

**CRITICAL DATES:** None

**SPECIAL INSTRUCTIONS:** None

**FILE NAME AND LOCATION:** S:\PSC\ECR\WP\060733.RCM.DOC

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### Case Background

Tampa Electric Company (“TECO” or “the Company”) requests authority from the Commission to use deferral accounting to create a regulatory asset or liability to recognize and offset the balance sheet treatment for pension and other postretirement benefit costs the company must record in accordance with Statement of Financial Accounting Standards (FAS) 158. The company also requests that the Commission acknowledge that if amounts represented by the establishment of such regulatory assets or liabilities were to be recognized in expense through a future curtailment, settlement or termination event pursuant to FAS 88 or FAS 106, the

recognized costs would be includable as a cost of service for ratemaking and surveillance purposes.

The Company's financial reporting is governed by Generally Accepted Accounting Principles, of which Financial Accounting Standards are a part. Several of these standards pertain to employee benefits as detailed below:

- FAS 87 prescribes the accounting treatment of defined benefit pension plans.
- FAS 88 prescribes the accounting treatment of settlements, curtailments and terminations of pension plans.
- FAS 106 prescribes the accounting treatment of other postretirement employee benefits (including settlements, curtailments and terminations of such plans).
- FAS 132R pertains to disclosure requirements for both pension and other postretirement benefit plans.
- FAS 158, issued on September 29, 2006, amends FAS 87, FAS 88, FAS 106 and FAS 132R by requiring employers to recognize the funded status of a benefit plan (measured as the difference between plan assets at fair value and the benefit obligation) in its statement of financial position. Previously, this information was only required to be disclosed in the footnotes to the employer's financial statements. For a pension plan, the benefit obligation is the projected benefit obligation; for any other postretirement benefit plan, such as a retiree health care plan, the benefit obligation is the accumulated postretirement benefit obligation. FAS 158 also requires employers to recognize the gains or losses and prior service costs or credits that arise during the period, but are not recognized as components of net periodic benefit cost pursuant to FAS 87 or FAS 106, as a component of other comprehensive income (an equity account), net of tax.
- FAS 71 allows regulated companies to defer costs and create regulatory assets provided the regulatory agency grants authority for such a deferral. As stated in the introduction to FAS 71:

Regulators sometimes include costs in allowable costs in a period other than the period in which the costs would be charged to expense by an unregulated enterprise. That procedure can create assets (future cash inflows that will result from the rate-making process), reduce assets (reductions of future cash inflows that will result from the rate-making process), or create liabilities (future cash outflows that will result from the rate-making process) for the regulated enterprise. For general-purpose financial reporting, an incurred cost for which a regulator permits recovery in a future period is accounted for like an incurred cost that is reimbursable under a cost-reimbursement-type contract.

Additional qualification requirements under FAS 71 are stated in Section 9 of FAS 71:

9. Rate actions of a regulator can provide reasonable assurance of the existence of an asset. An enterprise shall capitalize all or part of an incurred cost that would otherwise be charged to expense if both of the following criteria are met:
  - a) It is probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes.
  - b) Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred costs rather than to provide for expected levels of similar future costs. If the revenue will be provided through an automatic rate-adjustment clause, this criterion requires that the regulator's intent clearly be to permit recovery of the previously incurred costs.

TECO is seeking the Commission's approval of deferral accounting and acknowledgement of the likelihood of recovery of the previously incurred costs, in order to meet the requirements of FAS 71.

The Commission has jurisdiction pursuant to Sections 366.04, 366.06, and 366.07, Florida Statutes.

### **Discussion of Issues**

**Issue 1:** Should the Commission authorize Tampa Electric Company to use deferral accounting to create a regulatory asset or liability to recognize and offset the balance sheet treatment for pension and other postretirement benefit costs the Company must record in accordance with Statement of Financial Accounting Standards (FAS) 158?

**Recommendation:** Yes. The Commission should authorize Tampa Electric Company to use deferral accounting to create a regulatory asset or liability to recognize and offset the balance sheet treatment for pension and other postretirement benefit costs the Company must record in accordance with Statement of Financial Accounting Standards (FAS) 158. Further, the Commission should find that the approval to record the regulatory asset or liability for accounting purposes does not limit the Commission's ability to review the amounts for reasonableness in future rate proceedings. (Slemkewicz, Kyle)

**Staff Analysis:** Tampa Electric Company ("TECO" or "the Company") accounts for pension costs in accordance with FAS 87 and FAS 88, and for other postretirement benefit costs in accordance with FAS 106. The Commission has recognized FAS 87 and FAS 106 for ratemaking purposes. Essentially, this means that utilities must account for benefit plan costs using accrual accounting, as opposed to "pay-as-you-go" methods which were prevalent prior to the promulgation of the above standards. FAS 158, issued on September 29, 2006, amends FAS 87 and FAS 106 by requiring employers to recognize the funded status of a benefit plan (measured as the difference between plan assets at fair value and the benefit obligation) in its statement of financial position. For a pension plan, the benefit obligation is the projected benefit obligation, i.e. the actuarial present value of all benefits attributed by the pension benefit formula to employee service rendered prior to that date. For any other postretirement benefit plan, such as a retiree health care plan, the benefit obligation is the accumulated postretirement benefit obligation. FAS 158 also requires employers to recognize the gains or losses and prior service costs or credits that arise during the period, but are not recognized as components of net periodic benefit cost pursuant to FAS 87 or FAS 106, as a component of other comprehensive income (an equity account), net of tax.

FAS 71 allows regulated companies to defer costs and create regulatory assets, provided that it is probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes. To create a regulatory asset or liability, a regulated company must have the approval of its regulator. This concept of deferral accounting allows companies to defer costs due to events beyond their control and seek recovery through rates at a later time. The alternative would be for the company to seek a rate case each time it experiences an exogenous event.

The Company also requests that the Commission acknowledge that if amounts represented by the establishment of regulatory assets or liabilities were to be included in expense through a future curtailment, settlement or termination event pursuant to FAS 88 or FAS 106, the identified costs would be recognized as a cost of service for ratemaking and surveillance purposes.

Staff believes TECO's request to create a regulatory asset or liability to record charges that would otherwise have been recorded in equity under the provisions of FAS 158 meets the requirements of FAS 71 and should be approved. Further, staff believes that future recovery of costs resulting from curtailment, settlement or termination is implicit in a finding that FAS 71 is applicable. Finally, staff recommends that the Commission find that the approval to record the regulatory asset or liability for accounting purposes does not limit the Commission's ability to review the amounts for reasonableness in future rate proceedings.

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**Issue 2**: Should this docket be closed?

**Recommendation**: Yes. If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the Order, this docket should be closed upon the issuance of a Consummating Order. (M. Brown)

**Staff Analysis**: If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the Order, this docket should be closed upon the issuance of a Consummating Order.