

a patent application. The term includes preliminary investigations and detailed planning of specific projects for securing for customers non-conventional electric power supplies that rely on technology that has not been verified previously to be feasible. The term does not include expenditures for efficiency surveys; studies of management, management techniques and organization; consumer surveys, advertising, promotions, or items of a like nature.

32. *Retained Earnings* (formerly earned surplus) means the accumulated net income of the utility less distribution to stockholders and transfers to other capital accounts.

33. *Retirement units* means those items of electric plant which, when retired, with or without replacement, are accounted for by crediting the book cost thereof to the electric plant account in which included.

34. *Salvage value* means the amount received for property retired, less any expenses incurred in connection with the sale or in preparing the property for sale; or, if retained, the amount at which the material recoverable is chargeable to materials and supplies, or other appropriate account.

35. *Service life* means the time between the date electric plant is includible in electric plant in service, or electric plant leased to others, and the date of its retirement. If depreciation is accounted for on a production basis rather than on a time basis, then service life should be measured in terms of the appropriate unit of production.

36. *Service value* means the difference between original cost and net salvage value of electric plant.

37. *State* means a State admitted to the Union, the District of Columbia, and any organized Territory of the United States.

38. *Subsidiary Company* in the case of Major utilities means a company which is controlled by the utility through ownership of voting stock. (See *Definitions* item 5B, *Control*). A corporate joint venture in which a corporation is owned by a small group of businesses as a separate and specific business or project for the mutual benefit of the members of the group is a subsidiary

company for the purposes of this system of accounts.

39. *Utility*, as used herein and when not otherwise indicated in the context, means any public utility or licensee to which this system of accounts is applicable.

General Instructions

1. *Classification of utilities.*

A. For purpose of applying the system of accounts prescribed by the Commission, electric utilities and licensees are divided into classes, as follows:

(1) *Major*. Utilities and licensees that had, in each of the last three consecutive years, sales or transmission service that exceeded any one or more of the following:

(a) One million megawatt-hours of total sales;

(b) 100 megawatt-hours of sales for resale;

(c) 500 megawatt-hours of power exchanges delivered; or

(d) 500 megawatt-hours of wheeling for others (deliveries plus losses).

(2) *Nonmajor*. Utilities and licensees that are not classified as *Major* (as defined above), and had total sales in each of the last three consecutive years of 10,000 megawatt-hours or more.

B. This system applies to both Major and Nonmajor utilities and licensees. Provisions have been incorporated into this system for those entities which, prior to January 1, 1984, were applying the Commission's Uniform System of Accounts Prescribed for Public Utilities and Licensees subject to the Provisions of the Federal Power Act (Class C and Class D) [part 104 of this chapter, now revoked]. The notations (*Nonmajor*) and (*Major*) have been used to indicate those instructions and accounts from previous systems and classifications, which by definition, are not interchangeable without causing a loss of detail for the Major (previously Class A and Class B) or an increase in detail burden on the Nonmajor (previously Class C and Class D).

C. The class to which any utility or licensee belongs will originally be determined by its annual megawatt hours in each of the last three consecutive years, or in the case of a newly established entity, the projected data shall

be the basis. Subsequent changes in classification shall be made as necessary when the megawatt-hours for each of the three immediately preceding years shall exceed the upper limit, or be less than the lower limit of the classification previously applicable to the utility.

D. Any utility may, at its option, adopt the system of accounts prescribed by the Commission for any larger class of utilities.

2. *Records.*

A. Each utility shall keep its books of account, and all other books, records, and memoranda which support the entries in such books of account so as to be able to furnish readily full information as to any item included in any account. Each entry shall be supported by such detailed information as will permit ready identification, analysis, and verification of all facts relevant thereto.

B. The books and records referred to herein include not only accounting records in a limited technical sense, but all other records, such as minute books, stock books, reports, correspondence, memoranda, etc., which may be useful in developing the history of or facts regarding any transaction.

C. No utility shall destroy any such books or records unless the destruction thereof is permitted by rules and regulations of the Commission.

D. In addition to prescribed accounts, clearing accounts, temporary or experimental accounts, and subdivisions of any accounts, may be kept, provided the integrity of the prescribed accounts is not impaired.

E. All amounts included in the accounts prescribed herein for electric plant and operating expenses shall be just and reasonable and any payments or accruals by the utility in excess of just and reasonable charges shall be included in account 426.5, Other Deductions.

F. The arrangement or sequence of the accounts prescribed herein shall not be controlling as to the arrangement or sequence in report forms which may be prescribed by the Commission.

3. *Numbering System.*

A. The account numbering plan used herein consists of a system of three-digit whole numbers as follows:

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 expenses.
 900-949 Customer accounts, customer service and informational, sales, and general and administrative expenses.

B. In certain instances, numbers have been skipped in order to allow for possible later expansion or to permit better coordination with the numbering system for other utility departments.

C. The numbers prefixed to account titles are to be considered as parts of the titles. Each utility, however, may adopt for its own purposes a different system of account numbers (see also general instruction 2D) provided that the numbers herein prescribed shall appear in the descriptive headings of the ledger accounts and in the various sources of original entry; however, if a utility uses a different group of account numbers and it is not practicable to show the prescribed account numbers in the various sources of original entry, such reference to the prescribed account numbers may be omitted from the various sources of original entry. Moreover, each utility using different account numbers for its own purposes shall keep readily available a list of such account numbers which it uses and a reconciliation of such account numbers with the account numbers provided herein. It is intended that the utility's records shall be so kept as to permit ready analysis by prescribed accounts (by direct reference to sources of original entry to the extent practicable) and to permit preparation of financial and operating statements directly from such records at the end of each accounting period according to the prescribed accounts.

4. *Accounting Period.*

Each utility shall keep its books on a monthly basis so that for each month all transactions applicable thereto, as nearly as may be ascertained, shall be entered in the books of the utility. Amounts applicable or assignable to specific utility departments shall be so

segregated monthly. Each utility shall close its books at the end of each calendar year unless otherwise authorized by the Commission.

5. *Submittal of Questions.*

To maintain uniformity of accounting, utilities shall submit questions of doubtful interpretation to the Commission for consideration and decision.

6. *Item Lists.*

Lists of *items* appearing in the texts of the accounts or elsewhere herein are for the purpose of more clearly indicating the application of the prescribed accounting. The lists are intended to be representative, but not exhaustive. The appearance of an item in a list warrants the inclusion of the item in the account mentioned only when the text of the account also indicates inclusion inasmuch as the same item frequently appears in more than one list. The proper entry in each instance must be determined by the texts of the accounts.

7. *Extraordinary Items.*

It is the intent that net income shall reflect all items of profit and loss during the period with the exception of prior period adjustments as described in paragraph 7.1 and long-term debt as described in paragraph 17 below. Those items related to the effects of events and transactions which have occurred during the current period and which are of unusual nature and infrequent occurrence shall be considered extraordinary items. Accordingly, they will be events and transactions of significant effect which are abnormal and significantly different from the ordinary and typical activities of the company, and which would not reasonably be expected to recur in the foreseeable future. (In determining significance, items should be considered individually and not in the aggregate. However, the effects of a series of related transactions arising from a single specific and identifiable event or plan of action should be considered in the aggregate. To be considered as extraordinary under the above guidelines, an item should be more than approximately 5 percent of income, computed before extraordinary items. Commission approval must be obtained to treat an item of less than 5 percent, as extraordinary. (See accounts 434 and 435.)

7.1 *Prior period items.*

A. Items of profit and loss related to the following shall be accounted for as prior period adjustments and excluded from the determination of net income for the current year:

(1) Correction of an error in the financial statements of a prior year.

(2) Adjustments that result from realization of income tax benefits of pre-acquisition operating loss carryforwards of purchased subsidiaries.

B. All other items of profit and loss recognized during the year shall be included in the determination of net income for that year.

8. *Unaudited Items (Major Utility).*

Whenever a financial statement is required by the Commission, if it is known that a transaction has occurred which affects the accounts but the amount involved in the transaction and its effect upon the accounts cannot be determined with absolute accuracy, the amount shall be estimated and such estimated amount included in the proper accounts. The utility is not required to anticipate minor items which would not appreciably affect the accounts.

9. *Distribution of Pay and Expenses of Employees.*

The charges to electric plant, operating expense and other accounts for services and expenses of employees engaged in activities chargeable to various accounts, such as construction, maintenance, and operations, shall be based upon the actual time engaged in the respective classes of work, or in case that method is impracticable, upon the basis of a study of the time actually engaged during a representative period.

10. *Payroll Distribution.*

Underlying accounting data shall be maintained so that the distribution of the cost of labor charged direct to the various accounts will be readily available. Such underlying data shall permit a reasonably accurate distribution to be made of the cost of labor charged initially to clearing accounts so that the total labor cost may be classified among construction, cost of removed, electric operating functions (steam

generation, nuclear generation, hydraulic generation, transmission, distribution, etc.) and nonutility operations.

11. *Accounting to be on Accrual Basis.*

A. The utility is required to keep its accounts on the accrual basis. This requires the inclusion in its accounts of all known transactions of appreciable amount which affect the accounts. If bills covering such transactions have not been received or rendered, the amounts shall be estimated and appropriate adjustments made when the bills are received.

B. When payments are made in advance for items such as insurance, rents, taxes or interest the amount applicable to future periods shall be charged to account 165, Prepayments, and spread over the periods to which applicable by credits to account 165, and charges to the accounts appropriate for the expenditure.

12. *Records for Each Plant (Major Utility).*

Separate records shall be maintained by electric plant accounts of the book cost of each plant owned, including additions by the utility to plant leased from others, and of the cost of operating and maintaining each plant owned or operated. The term *plant* as here used means each generating station and each transmission line or appropriate group of transmission lines.

13. *Accounting for Other Departments.*

If the utility also operates other utility departments, such as gas, water, etc., it shall keep such accounts for the other departments as may be prescribed by proper authority and in the absence of prescribed accounts, it shall keep such accounts as are proper or necessary to reflect the results of operating each such department. It is not intended that proprietary and similar accounts which apply to the utility as a whole shall be departmentalized.

14. *Transactions With Associated Companies (Major Utility).*

Each utility shall keep its accounts and records so as to be able to furnish accurately and expeditiously statements of all transactions with associated companies. The statements may be required to show the general nature of the transactions, the amounts involved therein and the amounts in-

cluded in each account prescribed herein with respect to such transactions. Transactions with associated companies shall be recorded in the appropriate accounts for transactions of the same nature. Nothing herein contained, however, shall be construed as restraining the utility from subdividing accounts for the purpose of recording separately transactions with associated companies.

15. *Contingent Assets and Liabilities (Major Utility).*

Contingent assets represent a possible source of value to the utility contingent upon the fulfillment of conditions regarded as uncertain. Contingent liabilities include items which may under certain conditions become obligations of the utility but which are neither direct nor assumed liabilities at the date of the balance sheet. The utility shall be prepared to give a complete statement of significant contingent assets and liabilities (including cumulative dividends on preference stock) in its annual report and at such other times as may be requested by the Commission.

16. *Separate Accounts or Records for Each Licensed Project.*

The accounts or records of each licensee shall be so kept as to show for each project (including pumped storage) under license;

(a) The actual legitimate original cost of the project, including the original cost (or fair value, as determined under section 23 of the Federal Power Act) of the original project, the original cost of additions thereto and betterments thereof and credits for property retired from service, as determined under the Commission's regulations;

(b) The charges for operation and maintenance of the project property directly assignable to the project;

(c) The credits and debits to the depreciation and amortization accounts, and the balances in such accounts;

(d) The credits and debits to operating revenue, income, and retained earnings accounts that can be identified with and directly assigned to the project.

NOTE: The purpose of this instruction is to insure that accounts or records are currently

maintained by each licensee from which reports may be made to the Commission for use in determining the net investment in each licensed project. The instruction covers only the debit and credit items appearing in the licensee's accounts which may be identified with and assigned directly to any licensed project. In the determination of the net investment as defined in section 3 of the Federal Power Act, allocations of items affecting the net investment may be required where direct assignment is not practicable.

17. *Long-Term Debt: Premium, Discount and Expense, and Gain or Loss on Reacquisition.*

A. *Premium, discount and expense.* A separate premium, discount and expense account shall be maintained for each class and series of long-term debt (including receivers' certificates) issued or assumed by the utility. The premium will be recorded in account 225, Unamortized Premium on Long-Term Debt, the discount will be recorded in account 226, Unamortized Discount on Long-Term Debt—Debit, and the expense of issuance shall be recorded in account 181, Unamortized Debt Expense.

The premium, discount and expense shall be amortized over the life of the respective issues under a plan which will distribute the amounts equitably over the life of the securities. The amortization shall be on a monthly basis, and amounts thereof relating to discount and expense shall be charged to account 428, Amortization of Debt Discount and Expense. The amounts relating to premium shall be credited to account 429, Amortization of Premium on Debt—Credit.

B. *Reacquisition, without refunding.* When long-term debt is reacquired or redeemed without being converted into another form of long-term debt and when the transaction is not in connection with a refunding operation (primarily redemptions for sinking fund purposes), the difference between the amount paid upon reacquisition and the face value; plus any unamortized premium less any related unamortized debt expense and reacquisition costs; or less any unamortized discount, related debt expense and reacquisition costs applicable to the debt redeemed, retired and canceled, shall be included in account 189, Unamortized Loss on Reacquired Debt, or account 257,

Unamortized Gain on Reacquired Debt, as appropriate. The utility shall amortize the recorded amounts equally on a monthly basis over the remaining life of the respective security issues (old original debt). The amounts so amortized shall be charged to account 428.1, Amortization of Loss on Reacquired Debt, or credited to account 429.1, Amortization of Gain on Reacquired Debt—Credit, as appropriate.

C. *Reacquisition, with refunding.* When the redemption of one issue or series of bonds or other long-term obligations is financed by another issue or series before the maturity date of the first issue, the difference between the amount paid upon refunding and the face value; plus any unamortized premium less related debt expense or less any unamortized discount and related debt expense, applicable to the debt refunded, shall be included in account 189, Unamortized Loss on Reacquired Debt, or account 257, Unamortized Gain on Reacquired Debt, as appropriate. The utility may elect to account for such amounts as follows:

(1) Write them off immediately when the amounts are insignificant.

(2) Amortize them by equal monthly amounts over the remainder of the original life of the issue retired, or

(3) Amortize them by equal monthly amounts over the life of the new issue.

Once an election is made, it shall be applied on a consistent basis. The amounts in (1), (2) or (3) above shall be charged to account 428.1, Amortization of Loss on Reacquired Debt, or credited to account 429.1, Amortization of Gain on Reacquired Debt—Credit, as appropriate.

D. Under methods (2) and (3) above, the increase or reduction in current income taxes resulting from the reacquisition should be apportioned over the remainder of the original life of the issue retired or over the life of the new issue, as appropriate, as directed more specifically in paragraphs E and F below.

E. When the utility recognizes the loss in the year of reacquisition as a tax deduction, account 410.1, Provision for Deferred Income Taxes, Utility Operating Income, shall be debited and account 283, Accumulated Deferred Income Taxes—Other, shall be credited

with the amount of the related tax effect, such amount to be allocated to the periods affected in accordance with the provisions of account 283.

F. When the utility chooses to recognize the gain in the year of reacquisition as a taxable gain, account 411.1, Provision for Deferred Income Taxes—Credit, Utility Operating Income, shall be credited and account 190, Accumulated Deferred Income Taxes, shall be debited with the amount of the related tax effect, such amount to be allocated to the periods affected in accordance with the provisions of account 190.

G. When the utility chooses to use the optional privilege of deferring the tax on the gain attributable to the reacquisition of debt by reducing the depreciable basis of utility property for tax purposes, pursuant to section 108 of the Internal Revenue Code, the related tax effects shall be deferred as the income is recognized for accounting purposes, and the deferred amounts shall be amortized over the life of the associated property on a vintage year basis. Account 410.1, Provision for Deferred Income Taxes, Utility Operating Income, shall be debited, and account 282, Accumulated Deferred Income Taxes—Other Property shall be credited with an amount equal to the estimated income tax effect applicable to the portion of the income, attributable to reacquired debt, recognized for accounting purposes during the period. Account 282 shall be debited and account 411.1, Provision for Deferred Income Taxes—Credit, Utility Operating Income, shall be credited with an amount equal to the estimated income tax effects, during the life of the property, attributable to the reduction in the depreciable basis for tax purposes.

H. The tax effects relating to gain or loss shall be allocated as above to utility operations except in cases where a portion of the debt reacquired is directly applicable to nonutility operations. In that event, the related portion of the tax effects shall be allocated to nonutility operations. Where it can be established that reacquired debt is generally applicable to both utility and nonutility operations, the tax effects shall be allocated between utility and nonutility operations based on the ratio of net investment in util-

ity plant to net investment in non-utility plant.

I. Premium, discount, or expense on debt shall not be included as an element in the cost of construction or acquisition of property (tangible or intangible), except under the provisions of account 432, Allowance for Borrowed Funds Used During Construction—Credit.

J. *Alternate method.* Where a regulatory authority or a group of regulatory authorities having prime rate jurisdiction over the utility specifically disallows the rate principle of amortizing gains or losses on reacquisition of long-term debt without refunding, and does not apply the gain or loss to reduce interest charges in computing the allowed rate of return for rate purposes, then the following alternate method may be used to account for gains or losses relating to reacquisition of long-term debt, with or without refunding.

(1) The difference between the amount paid upon reacquisition of any long-term debt and the face value, adjusted for unamortized discount, expenses or premium, as the case may be, applicable to the debt redeemed shall be recognized currently in income and recorded in account 421, Miscellaneous Nonoperating Income, or account 426.5, Other Deductions.

(2) When this alternate method of accounting is used, the utility shall include a footnote to each financial statement, prepared for public use, explaining why this method is being used along with the treatment given for ratemaking purposes.

18. *Comprehensive Interperiod Income Tax Allocation.*

A. Where there are timing differences between the periods in which transactions affect taxable income and the periods in which they enter into the determination of pretax accounting income, the income tax effects of such transactions are to be recognized in the periods in which the differences between book accounting income and taxable income arise and in the periods in which the differences reverse using the deferred tax method. In general, comprehensive interperiod tax allocation should be followed whenever

transactions enter into the determination of pretax accounting income for the period even though some transactions may affect the determination of taxes payable in a different period, as further qualified below.

B. Utilities are not required to utilize comprehensive interperiod income tax allocation until the deferred income taxes are included as an expense in the rate level by the regulatory authority having rate jurisdiction over the utility. Where comprehensive interperiod tax allocation accounting is not practiced the utility shall include as a note to each financial statement, prepared for public use, a footnote explanation setting forth the utility's accounting policies with respect to interperiod tax allocation and describing the treatment for ratemaking purposes of the tax timing differences by regulatory authorities having rate jurisdiction.

C. Should the utility be subject to more than one agency having rate jurisdiction, its accounts shall appropriately reflect the ratemaking treatment (deferral or flow through) of each jurisdiction.

D. Once comprehensive interperiod tax allocation has been initiated either in whole or in part it shall be practiced on a consistent basis and shall not be changed or discontinued without prior Commission approval.

E. Tax effects deferred currently will be recorded as deferred debits or deferred credits in accounts 190, Accumulated Deferred Income Taxes, 281, Accumulated Deferred Income Taxes—Accelerated Amortization Property, 282, Accumulated Deferred Income Taxes—Other Property, and 283, Accumulated Deferred Income Taxes—Other, as appropriate. The resulting amounts recorded in these accounts shall be disposed of as prescribed in this system of accounts or as otherwise authorized by the Commission.

19. *Criteria for classifying leases.*

A. If at its inception a lease meets one or more of the following criteria, the lease shall be classified as a capital lease. Otherwise, it shall be classified as an operating lease.

(1) The lease transfers ownership of the property to the lessee by the end of the lease term

(2) The lease contains a bargain purchase option.

(3) The lease term is equal to 75 percent or more of the estimated economic life of the leased property. However, if the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease.

(4) The present value at the beginning of the lease term of the minimum lease payments, excluding that portion of the payments representing executory costs such as insurance, maintenance, and taxes to be paid by the lessor, including any profit thereon, equals or exceeds 90 percent of the excess of the fair value of the leased property to the lessor at the inception of the lease over any related investment tax credit retained by the lessor and expected to be realized by the lessor. However, if the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease. The lessee utility shall compute the present value of the minimum lease payments using its incremental borrowing rate, unless (A) it is practicable for the utility to learn the implicit rate computed by the lessor, and (B) the implicit rate computed by the lessor is less than the lessee's incremental borrowing rate. If both of those conditions are met, the lessee shall use the implicit rate.

B. If at any time the lessee and lessor agree to change the provisions of the lease, other than by renewing the lease or extending its term, in a manner that would have resulted in a different classification of the lease under the criteria in paragraph A had the changed terms been in effect at the inception of the lease, the revised agreement shall be considered as a new agreement over its term, and the criteria in paragraph A shall be applied for purposes of classifying the new lease. Likewise, any action that extends the lease beyond the expiration of the existing lease term, such as the exercise of a lease renewal option other than those already included in the lease term,

shall be considered as a new agreement and shall be classified according to the above provisions. Changes in estimates (for example, changes in estimates of the economic life or of the residual value of the leased property) or changes in circumstances (for example, default by the lessee) shall not give rise to a new classification of a lease for accounting purposes.

20. *Accounting for leases.*

A. All leases shall be classified as either capital or operating leases. The accounting for capitalized leases is effective January 1, 1984, except for the retroactive classification of certain leases which, in accordance with FASB No. 71, will not be required to be capitalized until after a three year transition period. For the purpose of reporting to the FERC, the transition period shall be deemed to end December 31, 1986.

B. The utility shall record a capital lease as an asset in account 101.1, Property under Capital Leases, Account 120.6, Nuclear Fuel under Capital Leases, or account 121, Nonutility Property, as appropriate, and an obligation in account 227, Obligations under Capital Leases—Noncurrent, or account 243, Obligations under Capital Leases—Current, at an amount equal to the present value at the beginning of the lease term of minimum lease payments during the lease term, excluding that portion of the payments representing executory costs such as insurance, maintenance, and taxes to be paid by the lessor, together with any profit thereon. However, if the amount so determined exceeds the fair value of the leased property at the inception of the lease, the amount recorded as the asset and obligation shall be the fair value.

C. Rental payments on all leases shall be charged to rent expense, fuel expense, construction work in progress, or other appropriate accounts as they become payable.

D. For a capital lease, for each period during the lease term, the amounts recorded for the asset and obligation shall be reduced by an amount equal to the portion of each lease payment that would have been allocated to the reduction of the obligation, if the payment had been treated as a payment on an

installment obligation (liability) and allocated between interest expense and a reduction of the obligation so as to produce a constant periodic rate of interest on the remaining balance.

21. *Allowances.*

A. Title IV of the Clean Air Act Amendments of 1990, Public Law No. 101-549, 104 Stat. 2399, 2584, provides for the issuance of allowances as a means to limit the emissions of certain airborne pollutants by various entities, including public utilities. Public utilities owning allowances, other than those acquired for speculative purposes, shall account for such allowances at cost in Account 158.1, Allowance Inventory, or Account 158.2, Allowances Withheld, as appropriate. Allowances acquired for speculative purposes and identified as such in contemporaneous records at the time of purchase shall be accounted for in Account 124, Other Investments.

B. When purchased allowances become eligible for use in different years, and the allocation of the purchase cost cannot be determined by fair value, the purchase cost allocated to allowances of each vintage shall be determined through use of a present-value based measurement. The interest rate used in the present-value measurement shall be the utility's incremental borrowing rate, in the month in which the allowances are acquired, for a loan with a term similar to the period that it will hold the allowances and in an amount equal to the purchase price.

C. The underlying records supporting Account 158.1 and Account 158.2 shall be maintained in sufficient detail so as to provide the number of allowances and the related cost by vintage year.

D. Issuances from inventory from inventory included in Account 158.1 and Account 158.2 shall be accounted for on a vintage basis using a monthly weighted-average method of cost determination. The cost of eligible allowances not used in the current year shall be transferred to the vintage for the immediately following year.

E. Account 158.1 shall be credited and Account 509, Allowances, debited so that the cost of the allowances to be remitted for the year is charged to expense monthly based on each month's

emissions. This may, in certain circumstances, require allocation of the cost of an allowance between months on a fractional basis.

F. In any period in which actual emissions exceed the amount allowable based on eligible allowances owned, the utility shall estimate the cost to acquire the additional allowances needed and charge Account 158.1 with the estimated cost. This estimated cost of future allowance acquisitions shall be credited to Account 158.1 and charged to Account 509 in the same accounting period as the related charge to Account 158.1. Should the actual cost of these allowances differ from the estimated cost, the differences shall be recognized in the then-current period's inventory issuance cost.

G. Any penalties assessed by the Environmental Protection Agency for the emission of excess pollutants shall be charged to Account 426.3, Penalties.

H. Gains on dispositions of allowances, other than allowances held for speculative purposes, shall be accounted for as follows. First, if there is uncertainty as to the regulatory treatment, the gain shall be deferred in Account 254, Other Regulatory Liabilities, pending resolution of the uncertainty. Second, if there is certainty as to the existence of a regulatory liability, the gain will be credited to Account 254, with subsequent recognition in income when reductions in charges to customers occur or the liability is otherwise satisfied. Third, all other gains will be credited to Account 411.8, Gains from Disposition of Allowances. Losses on disposition of allowances, other than allowances held for speculative purposes, shall be accounted for as follows. Losses that qualify as regulatory assets shall be charged directly to Account 182.3, Other Regulatory Assets. All other losses shall be charged to Account 411.9, Losses from Disposition of Allowances. (*See* Definition No. 30.) Gains or losses on disposition of allowances held for speculative purposes shall be recognized in Account 421, Miscellaneous Nonoperating Income, or Account 426.5, Other Deductions, as appropriate.

22. *Depreciation Accounting.*

A. *Method.* Utilities must use a method of depreciation that allocates in a

systematic and rational manner the service value of depreciable property over the service life of the property.

B. *Service lives.* Estimated useful service lives of depreciable property must be supported by engineering, economic, or other depreciation studies.

C. *Rate.* Utilities must use percentage rates of depreciation that are based on a method of depreciation that allocates in a systematic and rational manner the service value of depreciable property to the service life of the property. Where composite depreciation rates are used, they should be based on the weighted average estimated useful service lives of the depreciable property comprising the composite group.

23. *Accounting for other comprehensive income.*

A. Utilities shall record items of other comprehensive income in account 219, Accumulated other comprehensive income. Amounts included in this account shall be maintained by each category of other comprehensive income. Examples of categories of other comprehensive income include, foreign currency items, minimum pension liability adjustments, unrealized gains and losses on available-for-sale type securities and cash flow hedge amounts. Supporting records shall be maintained for account 219 so that the company can readily identify the cumulative amount of other comprehensive income for each item included in this account.

B. When an item of other comprehensive income enters into the determination of net income in the current or subsequent periods, a reclassification adjustment shall be recorded in account 219 to avoid double counting of that amount.

C. When it is probable that an item of other comprehensive income will be included in the development of cost-of-service rates in subsequent periods, that amount of unrealized losses or gains will be recorded in Accounts 182.3 or 254 as appropriate.

24. *Accounting for derivative instruments and hedging activities.*

A. Utilities shall recognize derivative instruments as either assets or liabilities in the financial statements and measure those instruments at fair

value, except those falling within recognized exceptions. Normal purchases or sales are contracts that provide for the purchase or sale of goods that will be delivered in quantities expected to be used or sold by the utility over a reasonable period in the normal course of business. A derivative instrument is a financial instrument or other contract with all of the following characteristics:

(1) It has one or more underlyings and a notional amount or payment provision. Those terms determine the amount of the settlement or settlements, and, in some cases, whether or not a settlement is required.

(2) It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors.

(3) Its terms require or permit net settlement, can readily be settled net by a means outside the contract, or provides for delivery of an asset that puts the recipient in a position not substantially different from net settlement.

B. The accounting for the changes in the fair value of derivative instruments depends upon its intended use and designation. Changes in the fair value of derivative instruments not designated as fair value or cash flow hedges shall be recorded in account 175, derivative instrument assets, or account 244, derivative instrument liabilities, as appropriate, with the gains recorded in account 421, miscellaneous nonoperating income, and losses recorded in account 426.5, other deductions.

C. A derivative instrument may be specifically designated as a fair value or cash flow hedge. A hedge is used to manage risk to price, interest rates, or foreign currency transactions. A company shall maintain documentation of the hedge relationship at the inception of the hedge that details the risk management objective and strategy for undertaking the hedge, the nature of the risk being hedged, and how hedge effectiveness will be determined.

D. If the utility designates the derivative instrument as a fair value hedge against exposure to changes in the fair value of a recognized asset, liability, or

a firm commitment, it shall record the change in fair value of the derivative instrument to account 176, derivative instrument assets-hedges, or account 245, derivative instrument liabilities-hedges, as appropriate, with a corresponding adjustment to the sub-account of the item being hedged. The ineffective portion of the hedge transaction shall be reflected in the same income or expense account that will be used when the hedged item enters into the determination of net income. In the case of a fair value hedge of a firm commitment a new asset or liability is created. As a result of the hedge relationship, the new asset or liability will become part of the carrying amount of the item being hedged.

E. If the utility designates the derivative instrument as a cash flow hedge against exposure to variable cash flows of a probable forecasted transaction, it shall record changes in the fair value of the derivative instrument in account 176, derivative instrument assets-hedges, or account 245, derivative instrument liabilities-hedges, as appropriate, with a corresponding amount in account 219, accumulated other comprehensive income, for the effective portion of the hedge. The ineffective portion of the hedge transaction shall be reflected in the same income or expense account that will be used when the hedged item enters into the determination of net income. Amounts recorded in other comprehensive income shall be reclassified into earnings in the same period or periods that the hedged forecasted item enters into the determination of net income.

Electric Plant Instructions

1. *Classification of electric plant at effective date of system of accounts (Major utilities).*

A. The electric plant accounts provided herein are the same as those contained in the prior system of accounts except for inclusion of accounts for nuclear production plant and some changes in classification in the general equipment accounts. Except for these changes, the balances in the various plant accounts, as determined under the prior system of accounts, should be