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CHAPTER I--FEDERAL ENERGY REGULATORY COMMISSION, DEPARTMENT OF ENERGY

General Instructions

1-1 *Classification of accounts*. Accounts are prescribed to record the cost of property used in transportation and related operations and for revenues, expenses, taxes, rents, and other items of income for such operations. Separate accounts are prescribed for cost of property not used in transportation operations and for income and expenses pertaining thereto; for other investments and related income; for extraordinary and prior period items, including applicable income taxes; and for assets and liabilities.

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In addition, stockholders' equity accounts, designed to segregate directly contributed capital from appropriated and unappropriated retained income, are provided. Retained income accounts form the connecting link between the income account and the equity section of the balance sheet. They are provided to record the transfer of net income or loss for the year; certain capital transactions; and, when authorized by the Commission, other items.

1-2 *Records*. (a) Carriers shall keep their accounts and records in accordance with the prescribed accounts. In addition, clearing accounts, temporary accounts, and subdivisions of any account may be kept provided the integrity of the prescribed accounts is not impaired. Each carrier 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 records, such as minute books, stock books, reports, correspondence, memorandums, etc., which may be useful in developing the history of or facts regarding any transaction.

(c) No carrier shall destroy any books, records, memoranda, etc., which support entries to its accounts unless destruction is permitted by the regulations governing preservation of records, Part 356 of this chapter. Starttime Thursday, April 15, 1999 15:38:11

(49 U.S.C. 5b, 304, 320, 904, 913, 917, 1003, 1012)

[32 FR 20241, Dec. 20, 1967, as amended at 40 FR 50384, Oct. 29, 1975. Redesignated and amended by Order 119, 46 FR 9044, Jan. 28, 1981]

1-3 *Accounting period*. (a) Each carrier shall keep its books on a monthly basis so that all transactions, as nearly as may be ascertained, shall be entered in the accounts not later than 60 days after the last day of the period for which the accounts are stated, except that the time within which the final entries for the year ending December 31 shall be made may be extended to such date in the following March as shall not interfere with the preparation and filing of the annual report.

(b) Changes shall not be made in the accounts for periods covered by reports that have been filed with the Commission unless the changes have first been authorized by the Commission.

1-4 *Accounting method*. (a) This system of accounts shall be kept by the accrual method of accounting. The basis used for accruing income and expense items each month shall be consistently applied and any change in such basis or any unusual accruals involving material amounts shall be promptly reported to the Commission.

(b) When the amount of any transaction cannot be accurately determined in time for inclusion in the applicable month's accounts, an estimated amount shall be entered in the proper accounts. Appropriate adjustments shall be made as soon as the actual amounts become known or at the time a substantial change is indicated. Carriers are not required to anticipate minor items which do not appreciably affect the accounts.

1-5 *Delayed items*. Ordinary delayed items and adjustments arising during the current year which are applicable to prior years shall be included in the same account which would have been charged or credited if the item had been taken up or the adjustments made in the year to which it pertained. When the amount of a delayed item or adjustment is relatively so large that its inclusion in net income for a single month would seriously distort the accounts for the month (but not for the year), such amount may be distributed in equal monthly charges or credits, as the case may be, to the remaining months of the calendar year. See instruction 1-6 for instructions covering extraordinary and prior period items of a nonrecurring nature.

1-6 Extraordinary, unusual or infrequent items, prior period adjustments, discontinued operations and accounting changes. (a) Extraordinary Items. All items of profit and loss recognized during the year are includible in ordinary

income unless evidence clearly supports their classification as extraordinary items. Extraordinary items are characterized by both their unusual nature and infrequent occurrence taking into account the environment in which the firm operates; they must also meet the materiality standard.

Unusual means the event or transaction must possess a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to the ordinary and typical activities of the entity.

Infrequent occurrence means the event or transaction shall be of a type not reasonably expected to recur in the foreseeable future.

(b) *Unusual or Infrequent Items*. Material events unusual in nature or infrequent in occurrence but not both, thus not meeting both criteria for classification as extraordinary, shall be includible in the accounts provided as separate components of income/expense from continuing operations. Such items are not to be reported net of income taxes.

(c) *Discontinued Operations*. The results of continuing operations shall be reported separately from discontinued operations and any gain or loss resulting from disposal of a segment of a business (see definition 32(a)) shall be reported in conjunction with the related results of discontinued operations and not as an extraordinary item. The disposal of a segment of a business shall be distinguished from other disposals of assets incident to the evolution of the entity's business, such as the disposal of part of a line of business, the shifting of production or marketing activities for a particular line of business from one location to another, the phasing out of a product line or class of service, and other changes occasioned by technological improvements. If a loss is expected from the proposed sale or abandonment of a segment, the estimated loss shall be provided for at the measurement date (see definition 32(b)). If a gain is expected, it shall be recognized when realized, which ordinarily is the disposal date (see definition 32(c)).

(d) *Prior Period Adjustments*. The correction of an error in the financial statements of a prior period and adjustments that result from realization of income tax benefits of preacquisition loss carryforwards of purchased subsidiaries shall be accounted for as prior period adjustments and excluded from the determination of net income from the current year. All other revenues, expenses, gains, and losses recognized during a period shall be included in the net income of that period.

(e) *Accounting Changes*. A change in accounting principle or accounting entity should be referred to this Commission for approval. The cumulative effect of a change in accounting principle should ordinarily be reflected in the account provided for in determining net income; in certain cases accounting changes may be reflected as prior period adjustments. Changes in accounting estimates should ordinarily be reflected prospectively.

(f) *Materiality*. As a general standard an item shall be considered material when it exceeds 10 percent of annual income (loss) before extraordinary items. An item may also be considered in relation to the trend of annual earnings before extraordinary items or other appropriate criteria. Items shall be considered individually and not in the aggregate in determining materiality. However, the effects of a series of related transactions arising from a single specific and identifiable event or plan

of action shall be aggregated to determine materiality.

(g) *Commission Approval and accountant's letter*. Items shall be included in the accounts provided for extraordinary items, unusual or infrequent items, discontinued operations, prior period adjustments and cumulative effect of changes in accounting principles only upon approval of the Commission. If the carrier retains the service of an independent accountant, a request for using these accounts shall be accompanied by a letter from the independent accountant approving or otherwise commenting on the request.

Note: The carrier may refer to generally accepted accounting principles for further guidance in applying instruction 1-6.

[40 FR 53248, Nov. 17, 1975. Redesignated by Order 119, 46 FR 9044, Jan.

28, 1981]

1-7 *Items in texts of accounts*. Items appearing in instructions and in the texts of various accounts are merely representative and are not intended to cover all of the items includible therein.

1-8 *Depreciation accounting--Carrier property*.

(a) *Method*. Monthly depreciation charges shall be made by the straight-line method to operating expenses in conformity with the group plan of accounting applicable to all carrier property except property included in accounts 101, 151, 171, Land, and 187, Construction Work in Progress.

(b) *Rates*. (1) Separate composite annual percentage rates will be prescribed for each depreciable account except that the Commission may authorize the use of component rates upon specific request from a carrier. Carriers becoming subject to this system of accounts and carriers acquiring property for which no rates have been previously prescribed shall file, within six months, composite annual percentage rates applicable to the book cost of each class of depreciable carrier property as will distribute the service value, by the straight-line method, in equal annual charges to operating expenses during the service life of the property. These rates shall be used by the carrier until the rates prescribed by the Commission become effective. Such rates shall, for each primary account comprised of more than one class of property, produce a depreciation charge equal to the sum of the amounts that would otherwise be chargeable for each of the various classes of property included in the account. Carriers shall base these percentage rates on estimated service values and service lives developed from engineering and other studies. The rates filed shall be accompanied by a statement showing the bases and the methods employed in the rate determination.

(2) Carriers shall be prepared at any time upon the direction of the Commission to compute and submit revised percentage rate studies. When a carrier believes that any rate prescribed by the Commission is no longer applicable, it shall submit the rate which it believes should be established supported by full particulars for consideration by the Commission.

(3) A carrier shall keep records of property and property retirements that will reflect the service life of property which has been retired, or will permit the determination of service life indications by mortality, turnover, or other appropriate methods; and also such records as will reflect the percentage of net salvage value for property retired from each class of depreciable carrier property.

(c) *Charges*. In computing monthly charges, the annual percentage rates shall be applied to the depreciation base as of the first of each month and the result divided by twelve.

(d) *Retirements*. Except as provided in paragraph (e) of this section, upon the retirement of depreciable property the service value shall be charged in its entirety to account 31, Accrued Depreciation--Carrier Property. Any amounts of insurance recovered from casualty losses involving depreciable property retired shall be credited thereto.

(e) *Special accounting authority*. (1) When circumstances indicate that newly acquired property should be subject to amortization, or that the prescribed depreciation rates based on the service lives of certain property are no longer applicable, because the source of traffic will be exhausted before the end of the physical service life, the carrier shall submit to the Commission for approval amortization or depreciation

rates based on the estimated remaining service life of the property accompanied by full information justifying the request.

(2) A carrier may request, or the Commission may direct, that special accounting be applied in situations causing undue inflation or deflation of depreciation reserves, such as premature or unusual retirements or sales of depreciable property, or related insurance recoveries. A carrier's request for special accounting shall contain full particulars concerning the situation, including the basis for its proposal. Alternative accounting techniques shall be applied to the extent approved or directed by the Commission.

1-9 *Depreciation accounting--Noncarrier property*. Monthly depreciation charges for all depreciable property recorded in account 34, Noncarrier Property, shall be made to account 620, Income from Noncarrier Property, with concurrent credits to account 35, Accrued Depreciation--Noncarrier Property. The depreciation charges shall be such as to distribute the service values equitably over the service life of the property.

1-10 *Amortization of intangibles*. Monthly charges shall be made to account 540, Depreciation and Amortization, to amortize the cost of fixed life intangibles such as permits, patents and franchises which are directly related to pipeline operations. Monthly charges shall be made to account 660, Miscellaneous Income Charges, to amortize the cost of intangibles such as goodwill which are not directly associated with pipeline operations. The amortization charges shall be such as to distribute the cost by the straight-line method in equal annual charges over the life or expected period of benefit.

1-11 *Interpretation of rules*. To maintain uniformity of accounting, carriers shall submit questions of doubtful interpretation to the Commission for consideration and decision.

1-12 *Accounting for income taxes*. (a) The interperiod tax allocation method of accounting shall be applied to all material temporary differences (see definition 30(e)) between the tax basis of an asset or liability and its reported amount in the financial statements that will result in taxable or deductible amounts in future years. Carriers may elect, as provided by the Revenue Act of 1971, to account for the investment tax credit by either the flow through method or the deferred method of accounting. See paragraphs (d) and (e) below. All income taxes (Federal, State, and other) currently accruable for income tax return purposes shall be charged to account 670, Income taxes on income from continuing operations, and account 695, Income taxes on extraordinary items, as applicable.

(b) Under the interperiod tax allocation method of accounting a deferred tax liability or asset is to be recognized for all temporary differences (see definition 30(e)) that result in taxable amounts in future years when the related asset or liability is recovered or settled. Deferred taxes are classified as current or noncurrent based on the classification of the related asset or liability. A carrier shall apply the applicable enacted tax rate in determining the amount of deferred taxes. The carrier shall adjust its deferred tax liabilities and assets for the effect of the change in tax law or rates in the period that the change is enacted. The adjustment shall be recorded in the proper deferred tax balance sheet accounts based on the nature of the temporary difference and the related classification requirements of the account.

(c) An entity shall record the income tax effects of a net operating loss carryforward or a tax credit carryforward as a deferred tax asset in the year the loss occurs. In the event that it is more likely than not (a likelihood of more than 50 percent) that some portion of its deferred tax assets will not be realized, a carrier shall reduce the asset by a valuation allowance. The valuation allowance should be recorded in a separate subaccount of the deferred tax asset account. The carrier shall disclose full particulars as to the nature and amount of each type of operating loss and tax credit carryforward in the notes to its financial statements. .

(d) Carriers electing to account for the investment tax credit by the flow through method shall credit account 670, Income taxes on income from continuing operations, or account 695, Income taxes on extraordinary items, as applicable, and charge to account 56,

Taxes payable, with the amount of investment tax credit utilized in the current accounting period. When the flow through method is followed for the investment tax credit, account 671, Provision for deferred taxes, shall reflect the difference between the tax payable (after recognition of allowable investment tax credit) based on taxable income and tax expense (with full recognition of investment tax credit that would be allowable based on accounting income) based on accounting income.

(e) Carriers electing to account for the investment tax credit by the deferred method shall concurrently with making the entries prescribed in (d) above charge account 671, ``Provision for deferred taxes'' or account 696, ``Provision for deferred taxes--extraordinary items,'' as applicable, and shall credit account 64, Accumulated Deferred Income Tax Liabilities with the investment tax credit utilized as a reduction of the current year's tax liability but deferred for accounting purposes. The investment tax credit so deferred shall be amortized by credits to account 671, ``Provision for deferred taxes''.

Note A: Any change in practice of accounting for the investment tax credit shall be reported promptly to the Commission. Carriers desiring to clear deferred investment tax credits because of a change from the deferral method to the flow through method shall submit the proposed journal entry to the Commission for consideration and advice.

Note B: The carrier shall follow generally accepted accounting principles where an interpretation of the accounting rules for income taxes is needed or obtain an interpretation from its public accountant or the Commission.

(Interstate Commerce Act, 49 U.S.C. 20 (1976), Department of Energy Organization Act, 42 U.S.C. 7155, 7172(b), 7295(a) (Supp. I 1977); E. O. 12009, 42 FR 46267 (1977); Federal Energy Regulatory Commission, Order No. 1, 42 FR 55450 (1977))

[39 FR 33344, Sept. 17, 1974, as amended at 40 FR 53247, Nov. 17, 1975; 44 FR 72161, Dec. 13, 1979. Redesignated by Order 119, 46 FR 9044, Jan. 28, 1981]

1-13 *Transactions with affiliated companies*. (a) The records and supporting data of all transactions with affiliated companies shall be maintained in a separate file. The types of transactions referred to in this paragraph are for management services or any other type of services rendered, sale or use of facilities or any other type of assets or property. The file shall be maintained so as to enable the carrier, to furnish accurate information with supporting documentation about particular transactions within 15 days of the request. We do not intend the file to include data relating to ordinary carrier operations (e.g. lawful tariff charges).

(b) Each bill rendered by an affiliated company shall state specifically the basis used for determining charges, unless the file contains other information to support the specific basis for charges.

(c) Punched cards, magnetic tapes, discs, or other machine-sensible device used for recording, consolidating, and summarizing accounting transactions and records with a carrier's electronic or automatic data processing system may constitute a file within the meaning of this instruction.

(d) The carrier shall record, as the cost of assets or services received from an affiliated supplier, the invoice price (plus any incidental costs related to those transactions) in those cases where the invoice price can be determined from a prevailing price list of the affiliated supplier available to the general public in the normal course of business. If no such price list exists, the charges shall be recorded at the lower of their cost to the originating affiliated supplier (less all applicable valuation reserves in case of asset sales), or their estimated fair market value determined on the basis of a representative study of similar competitive and arm's-length or bargained transactions.

Any difference between actual transaction price and the above, as well as charges that are not transportation related, shall be considered of a financing nature and shall be recorded, accordingly, as nonoperating charges or credits. (See Instruction 1-14).

(e) Nothing contained herein shall be construed as restraining the carrier from subdividing accounts (see Instruction 1-2(a)) for the purpose of recording

separately transactions with affiliated companies.

[40 FR 44562, Sept. 29, 1975. Redesignated by Order 119, 46 FR 9044, Jan. 28, 1981]

1-14 *Charges to be just and reasonable*. All charges to the accounts prescribed in this system of accounts for carrier property, operating revenues, operating and maintenance expenses, and other carrier expenses, shall be just, reasonable and not exceed amounts necessary to the honest and efficient operations and management of carrier business. Payments shall not exceed the fair market value of goods and services acquired in an arm's-length transaction. Any payments in excess of such just and reasonable charges shall be included in account 660, Miscellaneous Income Charges.

[40 FR 44562, Sept. 29, 1975. Redesignated by Order 119, 46 FR 9044, Jan. 28, 1981]

1-15 *Accounting for marketable equity securities owned*. (a) Accounts 11 ``Temporary investments,'' 20 ``Investments in affiliated companies,'' and 21 ``Other investments'' shall be maintained in such a manner as to reflect the marketable equity securities' portion (see definition 35) and other securities or investments.

(b) For the purpose of determining net ledger value, the marketable equity securities in account 11 shall be considered the current portfolio and the marketable equity securities in accounts 20 and 21 (combined) shall be considered the noncurrent portfolio. The net ledger value of each portfolio shall be the lower of its aggregate cost or market value. (See definition 35.) The amount by which aggregate cost exceeds market value shall be accounted for as the valuation allowance. Account 11 "Temporary investments" shall be subdivided to include the valuation allowance for the marketable equity securities included therein. Account 24 "Allowance for net unrealized loss on noncurrent marketable equity securities--Credit" is the valuation allowance for the marketable equity securities included in accounts 20 "Investments in affiliated companies" and 21 "Other investments." Marketable equity securities accounted for by the equity method shall not be combined with other marketable equity securities when determining aggregate cost and market value.

(c) Realized gains and losses (the difference between net proceeds from sale and cost) shall be included in income of the period in which they occur. Changes in the valuation allowance for marketable equity securities included in account 11 shall be charged to account 660 "Miscellaneous income charges" or credited to account 640 "Miscellaneous income" as appropriate, with a contra entry to the valuation allowance contained within account 11. Changes in the valuation allowance for marketable equity securities included in accounts 20 and 21 shall be recorded in equity account 75.5 "Net unrealized loss on noncurrent marketable equity securities" with a contra entry to valuation account 24.

(d) If there is a change in the classification of a marketable equity security between current and noncurrent, the security shall be transferred at the lower of its cost or market value at date of transfer. If market value is less than cost, the market value shall become the new cost basis, and the difference shall be accounted for as if it were a realized loss and included in the determination of net income.

(e) For long investments in marketable equity securities, when the decline in market value below cost is judged to be other than temporary, the cost basis of the individual security shall be written down to a new cost basis. The amount of the write-down shall be accounted for as a realized loss by a charge to account 660 "Miscellaneous income charges" and a credit to account 23, "Reduction in security values--Credit." The new cost basis shall not be changed for subsequent recoveries in value.

[42 FR 33297, June 30, 1977. Redesignated by Order 119, 46 FR 9044, Jan. 28, 1981]

1-16 *Accounting for inaccurate reporting of income taxes on income from continuing operations which occurred prior to reporting year 1979.* To the extent that any oil pipeline company, required to file annual reports with the Commission, did not correctly report State or other income taxes on continuing operations for the 1976, 1977, and 1978

reporting years, such company is ordered to disclose the amount of the accounting change in the space for notes and remarks provided in its 1979 Annual Report Form P, Schedule 300-A, of the Commission.

(Interstate Commerce Act, 49 U.S.C. 20 (1976), Department of Energy Organization Act, 42 U.S.C. 7155, 7172(b), 7295(a) (Supp. I 1977); E. O. 12009, 42 FR 46267 (1977); Federal Energy Regulatory Commission, Order No. 1, 42 FR 55450 (1977))

[44 FR 72161, Dec. 13, 1979. Redesignated by Order 119, 46 FR 9044, Jan. 28, 1981]