

GENERAL TERMS AND CONDITIONS

38. NEGOTIATED RATES (Continued)

38.6 Limitations

This Section 38 does not authorize Company to negotiate terms and conditions of service.

39. REGULATORY ACCOUNTING

39.1 Income Taxes

The term "income taxes" with respect to any period during which Company is organized as a partnership, shall be deemed to mean the amounts of income taxes which would have been paid or accrued if Company were organized during such period as a corporation, without limit as to negative or positive amounts of current or deferred income taxes. An allowance for federal and state income taxes, including current income taxes and provision for deferred income taxes, shall be computed in accordance with income tax accounting procedures which reflect the current and deferred tax consequences of all events that have been recognized in the financial statements or in taxable income, all as recorded in Account Nos. 409.1, before any reduction to reflect investment tax credit, 409.3 before any reduction to reflect investment tax credit, 410.1 and 411.1, including the amortization of any excess or deficient deferred income tax amounts applying the average rate assumption method, plus any interest received or paid on tax refunds or deficiencies, as recorded in Account Nos. 419 or 431.

GENERAL TERMS AND CONDITIONS

39. REGULATORY ACCOUNTING (Continued)

39.1 Income Taxes (Continued)

As used in this Subsection 39.1, "income tax accounting procedures which reflect the current and deferred tax consequences of all events that have been recognized in the financial statements or in taxable income" shall mean those procedures which require recording deferred tax liabilities and assets with a full provision for all income tax effects of all temporary differences and tax credit carryforwards.

A temporary difference is a difference 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 when the reported amount of the asset or liability is recovered or settled, respectively.

Company will allocate its interest expense to utility and non-utility activities for purposes of determining the provision for income tax in the cost of service by deducting, from the return allowance used to calculate the allowance for federal and state income taxes, only the utility portion of the debt component of return.

39.2 Settlement Adjustment Mechanism

Effective on the Billing Commencement Date of Service Agreements pursuant to Docket No. CP95-194, Company shall implement the Settlement Adjustment Mechanism ratemaking adjustment pursuant to the terms of the Stipulation and Agreement approved in Docket No. RP96-45 by means of memorandum accounting. The amount of the Settlement Adjustment Mechanism, initially \$31 million, shall be amortized using the Commission approved depreciation rate for Company's transmission plant and the effects of such amortization shall be an integral component of Company's cost of service calculation.

Issued by: Raymond D. Nepl, Vice President

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