



Public Service Commission ORIGINAL

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DATE: September 30, 1999
 TO: Linda Williams, Deputy Clerk Supervisor, Division of Records and Reporting
 FROM: Jay Revell, Regulatory Analyst, Division of Auditing and Financial Analysis *JR*
 RE: Docket No. 980643-EI - Generic investigation of cost allocation and affiliated transactions for electric utilities

Attached are comments from Gulf Power Company, that should be included in the above-referenced docket file.

JBR:slc
Attachment

- AFA _____
- APP _____
- CAF _____
- CMU _____
- CTR _____
- EAG _____
- LEG _____
- MAS _____
- OPC _____
- PAI _____
- SEC 1
- WAW _____
- OTH _____

DOCUMENT NUMBER-DATE

11830 SEP 30 89

FPSC-RECORDS/REPORTING

Gulf Power Company
Comments on the August 24, 1999 Proposed Rule Changes to Cost Allocation and Affiliated Transactions
Docket No. 980643-EI

General Comments

Gulf Power Company (Gulf) understands that the proposed rule amendments are modeled after the Telecommunications industry and the FPSC feels the proposed changes are necessary due to future deregulation of the electric utility industry. However, Gulf agrees with FP&L's position that there have been no documented abuses that need to be corrected and therefore; the proposed rule amendments are unnecessary and rulemaking changes should not proceed. The Commission has authority to review affiliated transactions at any time and has exercised that right. Affiliated transactions are also in the scope of the independent auditor's annual review of financial statements. The additional cost of resources required to adhere to the proposed rules may exceed any efficiency gained from affiliates using common resources and may discourage the most economical transaction. The proposed amendments are rigid, excessive, place a huge burden on the utilities and should not be adopted unless the Commission can clearly demonstrate the benefits. If the Commission adopts the proposed changes, they should not apply to transactions with regulated affiliates and parent / service companies regulated by the SEC. The pricing policy between a utility and affiliates of a holding company are already regulated by the Public Utility Holding Company Act of 1935 (PUHCA) which requires transactions to be made at cost. Transactions between parent / service companies and regulated utility affiliates are for the benefit of the utility ratepayer, not ventures into unregulated businesses.

As stated above, Gulf does not believe the proposed rule amendments are necessary. However, since the Staff's intentions are to pursue the proposed changes to the rule, Gulf offers the following comments, which are not inclusive and do not preclude future comments:

Purpose

The purpose of this rule is to establish reasonable and cost effective cost allocation guidelines and reporting requirements to ensure proper accounting for affiliate transactions and utility nonregulated activities so that these transactions and activities are not subsidized by rate payers, while promoting the efficient use of utility and affiliate resources. This rule is not applicable to affiliate transactions for purchase of fuel and related transportation services which are subject to Commission review and approval in cost recovery proceedings or to transactions with affiliates regulated by the SEC under the PUHCA or affiliates regulated by other State Public Service Commission's.

Explanation

Transactions between regulated utilities and / or a service co. regulated by PUHCA benefit the ratepayer by using common resources of which some are unique to the utility industry. For instance, many of the parts and materials used by the power plants and transmission and distribution are unique to utilities. By using a common material system, the holding company can reduce its subsidiaries cost of inventory and the cost of material systems. When a utility has an emergency need for a part, it can be obtained speedily from the affiliate at the affiliates cost. Requiring these type transactions to be subject to asymmetrical pricing or competitive bidding is not appropriate. These transactions between regulated affiliates and parent / service companies are not for diversification into unregulated ventures and should not be held to the proposed provisions of this rule.

(2) Definitions

Add definition

- (j) Cost effective affiliate transaction - "those transactions between affiliated companies that provide benefit to the regulated operation by either obtaining a product or service at less than other available alternatives or receiving a return on the provision of a product or service that provides for the recovery of expenses that would otherwise be absorbed by the regulated operation."

Words underlined are additions; words struck through are deletions from existing law; words in italics are comments.

Nonregulated and Regulated Definitions -- *Gulf concurs with FP&L's comments that the current definitions are confusing and suggests changing the definitions to be consistent with the NARUC as follows:*

~~Nonregulated - that which is not subject to regulation by regulatory authorities. The components of a utility's financial statements that are not taken into account in determining fair, just, and reasonable rates for utility service.~~

~~Regulated - that which is subject to regulation by regulatory authorities. The components of a utility's financial statements that are taken into account in determining fair, just, and reasonable rates for utility service.~~

(3) Non-Tariffed Affiliate Transactions — *Gulf concurs with FP&L's comments and proposed language changes to the title and purpose of (3) and (3) (a). In addition, Gulf believes that parent / service company and affiliated transactions with regulated utilities should be excluded from the scope of section (3) as these transactions are for the benefit of utility rate payers and are regulated by the SEC under the PUFCA. PUFCA requires transactions between the affiliates of a holding company to be priced at cost. Service companies provide specialized and administrative services to affiliates of which it would be difficult, costly, and impractical to obtain a comparable bid annually. In addition, these transactions are for the benefit of the regulated utility, not non-regulated ventures.*

(3) Non-Tariffed Affiliate Transactions Involving Regulated Activities

- a) The purpose of subsection (3) is to establish requirements for non-tariffed affiliate transactions involving regulated activities.
- b) A utility must charge an affiliate fully allocated costs for all non-tariffed regulated services and products purchased by the affiliate from the utility. Except, a utility may charge an affiliate less than fully allocated costs if the charge is above incremental cost and equivalent to market prices. If a utility charges less than fully allocated costs, the utility must maintain documentation to support doing so in accordance with the record retention requirements in Rule 25-6.014(3), F.A.C.
- c) A utility shall apportion to regulated operations the lesser of fully allocated costs or market price when purchasing services and products from an unregulated affiliate and applies the cost to regulated operations. If a utility apportions more than fully allocated costs to regulated operations, the utility must maintain documentation to support doing so in accordance with the record retention requirements in Rule 25-6.014(3), F.A.C. This section does not apply to transactions between affiliates of a holding company, which must be recorded at cost in accordance with PUFCA. Competitive bidding must be used when the utility projects to spend more than \$500,000 in a calendar year for a particular product or service.

Gulf agrees with FP&L's comments that the Commission has authority to protect utility customers from cross subsidization but does not have authority to set pricing standards over the utility's unregulated products and services. Therefore, section (3) b and c should be limited to regulated transactions.

(d) When an asset is transferred from between a utility to a nonregulated affiliate, the utility must charge the affiliate the greater of market or net book value, and an affiliate, the asset should be recorded by the utility at market value or cost if market value is not readily determinable. When an asset is transferred from a nonregulated affiliate to a utility, the utility must record the asset at the lower of market or net book value. An independent appraiser must verify the market value of a transferred asset with a net book value greater than \$1,000,000. This section does not apply to transactions between affiliates of a holding company, which must be recorded at cost in accordance with PUFCA.

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Gulf agrees with FP&L's comments that the rule should be limited in scope to assets that are related to the provision of regulated service and the Commission has no jurisdiction over nonregulated assets. As pointed out by EEI, "the asymmetric treatment of the unregulated affiliate that requires the "lower of market or fully allocated cost" for transactions in the opposite directions cannot be justified". This treatment could discourage the efficient use of resources between the utility and non-regulated affiliate. EEI suggests the use of an affiliate transfer pricing policy that protects the consumers of regulated services while promoting efficient use of utility and affiliate resources.

- (e) ~~Delete section (e) If an affiliate's accounts and records do not conform to the Uniform System of Accounts as prescribed by Rule 25-6.014, the utility must maintain a mapping system that reconciles the affiliate's account to the respective USOA accounts.~~

The affiliates should maintain their records so that charges to the utility can be supported. However, the utility should not be responsible for maintaining a mapping system that reconciles to the affiliate accounts. The utility's are not required to maintain a mapping system of non-affiliated vendors and does not see the benefit of a mapping system of affiliate's accounts. Gulf believes emphasis should be placed on the utility recording the transaction in the correct USOA account not where the affiliate recorded the original charge. The utility's chart of account should be adequate to determine if the transaction is regulated or non-regulated. Maintaining the mapping system will require perpetual updating, which will be costly and an unnecessary administrative burden.

- (f) *Limit to regulated affiliate. Each regulated affiliate involved in affiliate transactions must maintain all underlying data concerning the affiliate transaction for at least three years after the affiliate transaction is complete. This paragraph does not relieve a regulated affiliate from maintaining records under otherwise applicable record retention requirements.*

Commission does not have the authority to impose rules on non-regulated affiliates. In addition, non-regulated affiliates should not be subject to more regulatory requirements than non-affiliated vendors.

(4) Cost Allocation Principles —

- (d) *Delete section — EEI addressed the reporting requirement in the cost allocation manual (CAM) of annual revenue by each service or product. "Reporting requirements at this level of detail do not reflect current standard accounting practices. The inclusion of specific operational data of revenue by each service and product requires continual updating within the cost allocation manual which, by definition, is " an indexed compilation and documentation of a company's cost allocation policies and related procedure" -- not a financial report. In addition, requiring a utility to provide annual revenue breakdowns by each service and product provided to, or obtained from, a non-regulated affiliate is against standard industry practice, excessive, and therefore, costly."*

(5) Reporting Requirements—

(6) Audit Requirements —

Delete sections (b) (c) (d).

- (b) *Requiring an independent audit of affiliated transactions is excessive and costly. Internal Auditing reviews affiliated transactions periodically and affiliated transactions are within the scope of the independent auditor's annual review of the financial statements. The FPSC staff should be able to*

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conduct a compliance review of the CAM. The utility should not be burdened with additional audit requirements that are of questionable value.

- (c) *Reporting all incidents of non-compliance regardless of materiality is unreasonable.*
- (d) *Costs associated with the affiliated transactions audit should be chargeable to expense if it is a regulatory requirement. Disallowing a cost mandated by Commission rule is punitive.*

If Commission implements audit requirements, parent / service company and affiliated transactions with regulated utilities should be excluded from the additional audit requirements as these transactions are for the benefit of utility rate payers and are regulated by the SEC under the PUHCA. In addition, the SEC already requires an annual independent audit of the financial statements, which includes a review of the affiliated cost allocation methods. The service companies are required to have the cost allocation methods approved by the SEC. In addition, these transactions are for the benefit of the regulated utility, not non-regulated ventures and any audit costs should be recoverable from the utility ratepayers.

If (6) (b) is implemented, suggest the following changes:

Each utility shall file with the Commission an ~~audit report~~ attestation letter issued by an independent auditor commenting on the utility's compliance with its CAM. Beginning January 1, 2001, the ~~compliance audit attestation~~ shall be performed no less than once every three years in conjunction with the annual independent auditor's review of the financial statements. The ~~audit report attestation letter~~ shall be filed with the annual report or within 30 days of filing the annual report.

Annual Reports Section (2)

Delete this section

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