2019 Deloitte Power & Utilities Conference

Power is not static

Retrospective
Contents

- Opening address
- The not-so-static utility workforce
- Ratemaking trends and industry accounting
- Lease accounting update
- The evolving cyber risk and its collision with the power and utility industry
- NERC regulatory update
- SEC update
- Demystifying property tax for the controllership function
- To cloud or not to cloud: The future of ERP
- The evolving grid: An explanation of smart grid for the finance professional
- General accounting update
- XBRL for FERC reporting
- Powering the environmental, social, and governance (ESG) conversation
- Gaining insights: Geospatial and the utility
- After the storm: Lessons from recent events
- The questions that keep coming up
- Renewable accounting update
- Thank you

Click on session titles to go to the highlights.
The 2019 Deloitte Power & Utilities Conference took place in Chicago, Illinois, from December 3–4, 2019, and focused on learning and discussing the latest in technical accounting and reporting considerations and risk topics relevant to finance organizations, such as crisis response, cybersecurity, and much more.

Bill Graf, US Audit Power & Utilities leader and partner, Deloitte & Touche LLP, kicked off Deloitte’s Power & Utilities Conference by noting the change in location of the conference to downtown Chicago and to remind us to embrace our ever-changing environment. He emphasized that utilities are focused on customers, environment, safety, and political factors driving policy, which was discussed throughout the session.

This retrospective provides an overview of the memorable insights from the event, along with links to other conference materials.

“...utilities are focused on customers, environment, safety, and political factors driving policy”

Bill Graf, partner, Deloitte & Touche LLP
**The not-so-static utility workforce**

Brad Denny discussed the not-so-static utility workforce driven by conclusions reached and documented within the recently published 2019 Deloitte Human Capital Trends Report. The report states, “Power and utility leaders have recognized that, while businesses must generate a profit and deliver a return to shareholders, they must do so while also improving the lot of workers, customers, and the communities in which we live.” Brad explained that there have been several shifts in the industry that present potential risks if not addressed. These shifts include the need to adapt to technology’s pace of change, the decline of employee engagement, the need to prioritize safety while adapting to new ways of working, the inability to adapt to a nontraditional workforce, and the fact that utilities are not viewed as an attractive destination.

The shift from employee experience to human experience was identified as the No. 1 most important trend, as newer generations want more work/life balance and to understand how their work connects to the impact it has on the organization and society. About 57 percent of utility respondents said that they are good at creating meaningful work, but 58 percent of utility respondents are not satisfied with the way their work is designed. Companies should apply the same human experience that they provide to customers to their employees. There is also a tremendous amount of data available to help understand what employees need to do their jobs, and employees should be involved in redesigning their jobs, which would help retain and attract talent.

Talent mobility focuses on the idea that utilities can no longer expect to source and hire enough people with all the capabilities they require now and in the future; they must develop people internally to thrive. About 50 percent of leaders discourage their employees from moving into a new role. When trying to fill an open position, about 49 percent of leaders say that they don’t have the ability to see the skills that employees have internally. Career progression should also include moving from one area to another, not only moving up through the ranks. All levels and types of employees should have access to opportunities to move. The next steps utility companies need to make involve integrating the alternative workforce, improving the human experience for their employees, and developing talent and encouraging mobility.

**“About 50 percent of leaders discourage their employees from moving into a new role.”**

Brad Denny, principal, Deloitte Consulting LLP
Ratemaking trends and industry accounting

The panel focused its discussion on ratemaking trends and industry accounting topics and covered multiple scenarios involving unique regulatory issues, including abandonment, disallowances, and phase-in plans. Specifically on abandonments, if there is a reasonable chance the commission would not approve an early retirement of property, plant and equipment, then abandonment is likely not probable. If abandonment is considered probable, then the company must consider its potential for rate recovery to determine if there is a loss to record. Variations of an initial scenario demonstrated that companies need to continually assess probability and consider (1) relationships with the commission, (2) practices of the company to determine if they are comparable to a different company with a commission ruling, and (3) any other contradictory evidence that could affect the regulatory treatment for the company. Separately, regulatory orders received after period-end are normally considered a Type I subsequent event if they relate to contingencies existing at the balance sheet date.

A regulatory phase-in plan is a method of setting rates whereby costs related to a major, newly completed plant (such as depreciation and O&M) are reflected in rates more slowly than when those amounts are expensed under GAAP. When the method of setting rates is a phase-in plan, incurred costs cannot be deferred on the balance sheet as regulatory assets even if those costs are probable of recovery in future rates. There are a couple of exceptions to this accounting treatment of phase-in plans, which include instances where regulators use a specific method to set rates before 1982 (grandfathering), as well as if the deferral is solely due to regulatory lag. In these cases, the rate setting method is not considered a phase-in plan and a regulatory asset can be recorded.

Bill Graf, partner, Deloitte & Touche LLP
Tom Kilkenny, partner, Deloitte & Touche LLP
Amy Parker, partner, Deloitte & Touche LLP
Lease accounting update

James Barker discussed the following observations about adoption of the lease accounting standard. Qualitative disclosures were relatively light when they related to significant judgments used in applying ASC 842, including disclosure on the nature or type of leases, variable payment recognition, renewal or termination options, residual value guarantees, and judgments used in determining the discount rate. The majority of filers elected the practical expedient to combine lease and nonlease components and elected the package of practical expedients in ASC 842-10-65-1(f), but did not elect the hindsight practical expedient. Substantially, all companies utilized the “Comparatives Under 840 Option” transition method provided in ASU 2018-11.

Recent developments regarding the lease accounting standard include the deferral of the private company effective date to allow one extra year for adoption. Another recent development relates to the FASB’s views on collectability of operating lease receivables. Feedback from the FASB, which is acknowledged by the SEC, accepts use of a general reserve for uncollectible operating lease receivables, but does not require it. For companies that choose to utilize a general reserve, the FASB would accept establishment through lease revenue or through bad debt expense.

James also discussed that the implicit rate is required to be used by the lessee if it can be readily determined; however, the SEC believes that readily determinable is a very difficult requirement to meet, causing most companies to use the incremental borrowing rate. The incremental borrowing rate is lease-specific and reflects a collateralized borrowing rate. Lastly, James discussed a few industry hot topics, including lessee commencement loss resulting from significant variable payments, lessor accounting for maintenance expenditures under sales-type leases, and leases associated with AROs. Lessor commencement loss resulting from significant variable payments may require companies to record a loss at commencement date for profitable lease arrangements. This issue is often encountered in the renewable sector particularly on projects accompanied by battery storage. EEI has made a formal request to the FASB to make an exception that allows these leases to be treated as operating leases; the request is expected to be considered in 2020. In the meantime, companies may consider non-GAAP measures to explain the anomalous results. Lessor accounting for maintenance expenditures under sales-type leases is applicable to many long-term PPAs, where the plant is “sold” to an off-taker and a supplier agrees to provide O&M services over the PPA term. Capital expenditures incurred to satisfy a performance obligation to the lessee will generally be expensed, and capital expenditures incurred during the PPA term, but for the benefit of the lessor, will likely qualify for capitalization in many circumstances. Leases associated with AROs, where the company enters into a lease to fulfill an ARO obligation, will often be accounted for as two separate liabilities. To avoid over-expensing, the ROU asset associated with the lease should be reduced as the ARO liability is reduced.

“Recent developments regarding the lease account standard include the deferral of the private company effective date to allow one extra year for adoption.”

James Barker, partner, Deloitte & Touche LLP
Jim Turgal suggested the audience look at cyber risk as the following concepts: data, ecosystems, and attack surfaces. For example, the interconnection of the devices within our homes is an ecosystem, an attack surface is every device (for example, each phone, tablet, or smart TV) within the ecosystem, and the data is everything that is transmitted between the interfaces.

He explained that threat actors include cybercriminals, customers, employees, contractors, and state actors, among others. In addition, vectors (for example, phishing) refer to vehicles for accessing data. Understanding how threat actors may attack is critical, especially given the number of attack surfaces within the power and utilities industry (for example, substations and smart meters).

According to Jim, a cyber breach occurring at every entity is not a matter of if, but when. Being prepared for a cyber breach requires extensive internal communication within an organization, cohesiveness, and a consistent way of thinking about cyber risks amongst every member of the organization. Organizations must be aware of where they are most vulnerable, including defining their most vulnerable data. Simplification, automation, change management, and third-party interaction are important aspects of cyber strategy evolution. Simplification can reduce the number of attack surfaces. It is important to understand the entire infrastructure of one’s networks so that risks and gaps can be identified and a cyber strategy can be implemented. Third parties with which an entity interacts are often the biggest threat.

It’s habitual to analyze the financial statements of an acquiree in a potential acquisition, but entities should consider the IT infrastructure of an acquiree (for example, the acquirer’s patch management strategy) because breaches often follow acquisitions or mergers. In addition, it was reiterated that C-suite individuals and directors are having to take financial responsibility, via shareholder lawsuits, instances where a company doesn’t appropriately handle cyber breaches.
NERC regulatory update

Dmitriy Borovik presented the upcoming and in-flight NERC requirements, including CIP-013-1, CIP-005-6, and CIP-010-3, related to supply chain risk management. He explained that NERC issued a standard to ensure security and prevent issues within the bulk electric system infrastructure. NERC plans to bring low-impact assets into the regulatory landscape (for example, wind and solar renewable facilities) so that they will have to comply with NERC reliability standards. Subcomponents, components, and major systems were discussed related to cyber supply chain risk management. The audience learned that cyber supply chain issues typically stem from the risk that compromised or counterfeit components could enter the chain from lower tiers, which are less visible to utilities.

Mechelle Thomas joined the discussion and shared her perspectives related to the overall NERC philosophy, lessons learned on her journey to becoming chief compliance officer and since, and challenges NERC is facing, which included cyber and preparing the bulk power system for cyberattacks. She also discussed how entities can achieve NERC compliance in their procurement processes.

“Cyber is complex and scary.”

Dmitriy Borovik, managing director, Deloitte & Touche LLP
Mechelle Thomas, Vice President and Chief Compliance Officer, NERC
SEC update

Dave Horn discussed SEC priorities and rulemaking, including final rules issued, proposed rules, those rules that are in the request for comment phase, and what is on the horizon. He explained that certain SEC efforts relate to streamlining requirements reducing duplication within authoritative literature. Rules that are decades old require change because of new technologies and due to changing expectations of constituents. There are three key areas of emerging risk disclosures: (1) cyber (including tailored and timely disclosures if there is a breach, the impact to the organization, and information related to remediation efforts), (2) Brexit, and (3) LIBOR transition. The SEC has been focused on SAB 74 disclosures. The cadence of quarterly reporting may not ever be added to the SEC’s agenda, but the question was raised by the president.

The key provisions of the FAST Act were presented. Aspects of the proposed rule related to acquired and disposed business financial information were discussed, including measuring significance, acquiree financial statements, pro forma financial information, and other key changes. In addition, proposed rules related to accelerated and large accelerated filers, as well as business, legal proceedings, and risk factor disclosures, were discussed.

Andrea Perdomo presented information related to the disclosure program realignment, which included the realignment into four groups: (1) disclosure review, 2) specialized policy and disclosure, (3) risk and strategy, and (4) assessment and continuous improvement. Andrea indicated that we don’t yet know the full effect of the realignment, but that we do know personnel will still leverage industry experience as they are reviewing filings.

The SEC review process was highlighted, and information related to declining comment letter trends was presented. Andrea explained that non-GAAP measures still top the list of top 10 comment letter trends, with revenue recognition coming in at No. 2. Revenue recognition would be No. 1 if the list were quantified based the number of individual comments, rather than the number of filings that contained a comment related to revenue recognition.
Demystifying property tax for the controllership function

Debbie Loesel discussed what might be useful for accounting and finance professionals to know about property taxes. She discussed why property taxes don't necessarily behave in the way you think they will. Statistics related to state and local general revenues were presented, with property tax revenues representing 34 percent of the total state and local general revenues on average nationally in 2016. Property tax revenues were greater than corporate income tax and individual income tax revenues combined.

Regarding state and local tax revenues, property tax as a percentage of overall state and local tax revenue was between 28 percent and 35 percent over the 2000–2016 time period. While there are some peaks and valleys, the general trend is upward. Increased property taxes can be levied in periods where other taxes are down due to their formulaic nature (and they would be increased to fulfill revenue requirements of state and local governments).

Assessed value for property tax purposes may not necessarily equal fair market value and is typically fair market value as adjusted for assessment ratios and/or equalization rates. The tax rate applies to assessed value. The property tax value of an asset is generally not equal to the net book value of the asset.

There can be significant lag and variation in the property tax assessment cycle. The lag can create challenges in budgeting and forecasting and understanding whether large capital expenditure projects have been reflected in the property tax liability. The variation in taxing authority's fiscal years between states, and even within states, increases difficulty with accruals, as the preferred accrual period is the taxing authority's fiscal year. Data and reporting considerations were discussed, including location, cost elements, and land changes.

“Property tax revenues were greater than corporate income tax and individual income tax revenues combined.”

Debbie Loesel, senior manager, Deloitte Tax LLP
To cloud or not to cloud: The future of ERP

“There isn’t a choice, as the cloud journey is here,” explained Eli Black. He mentioned that we are already on the second wave of the cloud journey. Artificial intelligence and cognitive technological advancements have enabled us to get more out of information and get more value from our data. In addition, vendors are adopting cloud technology, and we are starting to see the full potential of the cloud.

Employees don’t want to be bound by the same systems and processes, and customers want more from their power and utility providers. Eli explained that we are moving to a model with prebuilt systems that can be enabled at the click of a mouse. Historically, IT infrastructure could have taken weeks, months, or even years to install.

The audience learned that the way IT infrastructure was previously implemented (manual configuration and utilization of a data center) doesn’t quite work in adopting cloud technology. Adopting cloud technology doesn’t necessarily make one more secure if it’s not configured appropriately. The cybersecurity focus needs to shift, as new risks are introduced by the cloud. Moving to the cloud needs to go beyond lift and shift, and organizations are challenged managing their cloud migration journey.

Implementing an effective strategy will enhance governance and reduce risks and cloud adoption comes with cyber risk challenges that should be addressed. For example, risks and controls may not be aligned to industry standards and leading practices and incorporation of cloud into existing governance processes and operational workflows may be disruptive. Eli emphasized the importance of understanding your cloud governance and controls across cyber security domains. In addition, the importance of security capabilities at implementation being blueprinted were also discussed. The path to a secure cloud is not straightforward. There are certain milestones to track in the journey to secure the cloud and transformation can begin with focusing on a few important areas.
Dr. Mani Vadari led a discussion on smart grid. He provided background on the beginning of the modern electrical grid, which originated in Manhattan. Over time, the grid evolved to include centralized generation, transmission, distribution, and the end-user customer. In the mid-1990s, the Federal Energy Regulatory Committee (FERC) set up wholesale energy markets across the country that are still successfully operating today. The “smart grid” emerged in the early 2000s, when new terms and technologies emerged, such as distributed energy, microgrids, smart homes, and data analytics.

Mani explained that changes are afoot where distributed energy resources (DER) are becoming more viable in terms of cost, performance, and reliability and come with increased levels of dispatchability. The price of storage is coming down to a level that, when combined with DERs, allows customers, aggregators, or an incumbent utility to deliver energy where and when it is needed. Distribution automation supported by decision mechanisms allows stakeholders both within and outside the utility a full suite of situational awareness tools. Microgrids are formed when parts of the grid are spun off into their own semi-independent entities and interact with utility, either during a steady state, emergency situations, or never. Homes and buildings become truly smart with nanogrid-like controls with an increased level of automation, connecting over the cloud with reduced need for customer involvement.

For electric utilities, this is a tough place, as everything under them is shifting. Distributed energy allows the customer to produce energy and either use it for themselves or sell it back to the utility. Storage allows anyone to store energy when it is plentiful and cheap and release it when it is not. Microgrids allow a group of homes, offices, or industries to manage their own electric needs, whether still connected to the electric grid or not. Electric vehicles are becoming more relevant, bringing a completely new type of load to the electric grid. Homes and buildings are becoming smarter, thereby allowing for the control of their consumption and generation if available. A new genre of automation is becoming available, enabling improved sensing and control of everything in the grid and beyond the meter.

Lastly, Dr. Mani listed characteristics of a transformed utility, which include having a flexible operating model, focus on the customer and their desires, managed DERs, redefined planning and asset management, data and digital insights, and the willingness to embrace change and innovate to turn threats into opportunities.
General accounting update

Chris Lee led a general accounting update and presented on the following topics: cloud computing, CECL, the balance sheet classification of debt, and service concession arrangements. He also provided an update on critical audit matters (CAMs).

Regarding cloud computing, Chris provided a refresher on ASU 2015-05, clarifying when software hosted by a third party is a software license or a service contract. If users can take possession and feasibly operate on their own system, the arrangement contains a license. If not, the arrangement is a service contract. The issue with ASU 2015-05 was that it gave limited guidance on accounting for the cost of implementation activities for service contracts. ASU 2018-15 was issued in 2018 and is effective for public companies for the year ended December 31, 2020. The main provision of the update was to align cloud computing implementation costs for a service contract with the rules for internal-use software. Eligible costs to capitalize include other software for conversion, external costs of conversion (consultants), and internal personnel costs for conversion. Ineligible costs include data cleansing, classifying, preprocessing, training, and maintenance. This guidance impacts implementation costs only. All other cloud costs are expensed as incurred, typically as an element of operations and maintenance expense. The audience learned that capitalized costs are amortized over the life of the arrangement, including options, if those operations are reasonably certain of exercise. Also, it is important to consider if legacy systems need to be assessed for impairment if they're no longer in use as a result of transitioning to the cloud.

Chris also led a discussion on Current Expected Credit Loss (CECL). This is the new accounting standard related to credit losses for financial assets. It is a complicated standard; however, it is expected to be far less impactful to the power and utilities industry than other industries. None of the multiple impairment models under current GAAP required a preparer to consider credit of the counterparty and as a result, there was great diversity in how financial assets were valued. He reiterated that the CECL model is an expected loss model, as opposed to an incurred loss model. Credit losses under the CECL model are recognized based on historical experience, current conditions, and reasonable forecasts. Trade receivables and unbilled revenues are generally where P&U companies will see an impact from CECL. Companies should also pay careful attention for insurance receivables and debt guarantees as they implement the standard.

Next, Chris presented on the FASB's project related to the balance sheet classification of debt. The current guidance in ASC 470-10 is very fact-specific with many exceptions, and the goal of this project is to simplify this guidance by introducing a principles-based, common sense approach which considers intent and ability to refinance as well as the status of covenant violations and related waivers.

Service concession arrangements are contracts whereby a government or other body (the grantor) grants contracts for the supply of public services on behalf of the grantor. These types of arrangements are also known as public private partnerships and examples include toll roads, prisons, national parks and hospitals. There are numerous examples where energy companies could enter into arrangements to provide public services. Typically for an energy company, these arrangements would involve constructing then operating an asset on behalf of a government entity. There was new guidance in 2018 in connection with ASC 606 related to service concession arrangements. In general, companies need to follow a percentage of completion method of accounting for revenue recognition and be mindful of milestones for phases of projects which may have different margins.
XBRL for FERC reporting

Nicole Shaw and Neritan Xhaferi discussed the adoption of the XBRL standard at FERC and the XBRL implementation and preparation that companies should be considering in adopting this new standard. FERC will adopt the XBRL standard for all filers submitting Forms 1, 1-F, 2, 2-A, 3-Q, 6, 6-Q, 60, and 714 in 2021. FERC adopting the XBRL standard supports a standards-based method which allows customers to prepare, publish, and exchange information in a variety of formats. The standard offers cost savings, greater efficiency, and improved accuracy in supplying informational data as well as increased transparency to all stakeholders at a granular level. The XBRL standard provides a language in which all the reporting elements that make up the FERC forms can be authoritatively defined, to render analysis across all filers possible.

In early 2020, FERC will convene a staff-led technical conference to walkthrough the XBRL taxonomy and finalize the XBRL implementation timeline and expected implementation is Q2 2021. FERC’s standard taxonomy will be publicly available to map elements into the company’s XBRL file, and filers will submit via FERC’s online web portal. The most significant impact will be experienced in the year of implementation as there is expected to be a significant effort to review the appropriate tag selection and additional software or vendor costs will be incurred to build the taxonomy. Companies should perform a FERC taxonomy review, assemble a team, and assess the current technology environment to prepare for the XBRL adoption.

“Companies should perform a FERC taxonomy review, assemble a team, and assess the current technology environment to prepare for the XBRL adoption.”

Nicole Shaw, manager, Deloitte & Touche LLP
Neritan Xhaferi, manager, Deloitte & Touche LLP
Powering the environmental, social, and governance (ESG) conversation

Christine Robinson led the conversation around environmental, social, and governance and how factors affect sustainability for utility companies. Market pressures from multiple parties are driving transparency when it comes to sustainability at electric and gas companies. Investors are engaging with the largest corporate greenhouse gas emitters to strengthen climate-related disclosures and divesting in unsustainable energy, such as coal. Credit raters are incorporating ESG into credit analysis, causing lenders and insurers to be less likely to partner with unsustainable companies. There are currently no policy disclosure requirements; however, cities have been committing to achieve 100 percent renewable energy. About 64 percent of employees won’t take a job if the company does not have strong social responsibility values. Directors and boards are focusing more on sustainability, and standard-setters are working on how companies should disclose sustainability.

Studies have shown that firms with good performance on “material sustainability issues” and concurrently poor performance on “immaterial sustainability issues” enjoy the strongest financial returns. The World Economic Forum’s 2019 Global Risks Report shows that many ESG factors, such as extreme weather events, failure of climate-change mitigation and adaption, and natural disasters were identified as high risks for companies. The New Energy Outlook 2019 published by Bloomberg presents a timeline where coal peaks globally in 2026 and there is more wind and solar electricity in the world than coal-fired electricity by 2032. The report estimates that by 2035, utility-scale batteries for peaking purposes start growing in significance and by 2050, US power sector emissions decline by 54 percent, global power demand grows by 62 percent, coal only supplies 12 percent of world electricity, and peaking gas plants increase by 350 percent.

“About 64 percent of employees won’t take a job if the company does not have strong social responsibility values.”

Christine Robinson, senior manager, Deloitte & Touche LLP
Gaining insights: Geospatial and the utility

Robert Renner led a discussion on location intelligence and leveraging the power of where to reveal insights from your enterprise data. He discussed geospatial data, which includes things like facilities, routes, customer addresses, and GPS locations. Location intelligence uses spatial analysis to perform proximity or statistical analyses to detect patterns or trends and visualizations to view assets with other data. Geospatial analytics includes the collection, visualization, and analysis of data that can be tied to a geographic location on, above, or below the Earth's surface. Geographic information systems are critical to any utility's business, and location information is at the heart of almost everything you do in utilities—from field operations to financial analytics.

He also discussed how location intelligence can also be used by utilities to understand the impact of storm surge and flood risk on the utility infrastructure. There are many relevant data sources and tools available to help model and quantify risk from hurricanes and major storms to utilities and other types of critical infrastructure, including LiDAR imagery, SLOSH models, land use and land cover data, and Federal Energy Management Agency (FEMA) floodplain boundaries. After major storms, FEMA and their partners in federal and state agencies publish massive volumes of spatial data.

Geospatial technology provides a location-based view of an organization’s footprint. When combined with data from multiple sources, this information can be used to understand where risks may occur, analyze various mitigation techniques, and monitor risks and risk management actions over time.

“Geospatial technology provides a location-based view of an organization’s footprint”

Robert Renner, specialist leader, Deloitte & Touche LLP
After the storm: Lessons from recent events

In this session, Sarah Lawrence and Kathryn Schwerdtfeger discussed crisis management and some of the lessons learned through major catastrophic events, including fires and hurricanes. The characteristics of a crisis describe something that is bigger than normal, that rapidly evolves, and that has especially high stakes.

What we know is crises are happening more frequently, with greater complexity and severity. Cyberattacks are happening more often as our reliance on technology increases and financial disruptions are happening more frequently. We are at a time where the level of confrontations is coming at us much more rapidly. Huge spikes in disasters were not only attributable to hurricanes. Environmental changes, economic change and urbanization have contributed to rising natural disasters. Concrete urbanization and poor drainage exacerbated problems in certain cases. Storms are getting bigger, faster and more destructive. Regarding natural disasters, the concept of a volatility, uncertainty, complex, and ambiguity (VUCA) environment, which is an environment that is volatile, uncertain and complex, was introduced. Leaders are starting to use the term, VUCA environment, to explain the level of chaos that we have in the business world today. The question is how one gets better at predicting what we don’t know. The amount of information needed and the things we must do to respond to these events to get back up and running is very difficult. We are dealing with ambiguity which requires doing things in a way we haven’t had to before.

Sarah and Kathryn discussed what survey respondents said they’ve learned about navigating recent crisis events. Leaders needing more development for crisis management was emphasized. No one is ever perfectly prepared in this situation, but being ready significantly reduces the negative impact. We all need third parties to assist in a crisis, and figuring out how to use third parties to your advantage to make them solutions, and not problems, is critical. After a crisis, companies admitted that there were things they absolutely did not do very well. The first thing they said was they got so myopic in getting the lights back on that they forgot the near-term and long-term impacts to strategy. They also said they underestimated the magnitude. Organizations need to step back and say what could happen in my environment. Everyone thinks their current leadership team is the right team to manage anything that can happen to the company, but they’re learning afterward that that isn’t always the case. The very people that get the operations up and running in a crisis may not be the same people that are best at communicating to stakeholders. Some respondents mentioned that the biggest mistake they made was they weren't on the same page about the facts, and the scripts were different (causing issues with communications to stakeholders). It is about communication and making sure the right people are in the right place.

During a crisis management life cycle, every part of the business must be involved. You must create a culture thinking through what potentially can happen. One can’t keep doing it the old way, because these events are bigger and faster. We are learning now that people don’t leave, so you must assess how you create a place to live. There are large corporations which, during a crisis, simply do not have workers, because those workers have no place to live and don’t have the money to commute from a distant location. Communities and companies must think differently.
Eileen Little discussed frequent areas of rate-regulated accounting consultations for 2019, including FERC hot topics. The accounting for regulatory assets and liabilities often involves significant management judgments and estimates. In terms of regulatory assets, she noted that questions continue to arise related to assessing the likelihood of future recovery, particularly in situations where there is a lack of precedent. Other common consultation topics include disallowance considerations (assessing if a disallowance is probable), abandonments (balance sheet presentation and evaluation of cost recovery), and netting considerations for regulatory assets and liabilities (what is the unit of account?). She discussed that the accounting for tax-related regulatory assets and liabilities continued to be a hot topic throughout 2019 as entities worked with their respective commissions on the method and timing for the return of excess federal deferred income taxes to customers. She wrapped up this portion of her session noting that a continued theme in 2019 rate case activity involves rate mitigation for customers, and we are more commonly seeing commissions have a greater focus on prudency and a higher incidence of various types of cost disallowances. This in turn has led to more complex accounting evaluation for potential disallowances for both recently completed plant or plant under construction as well as for other costs deferred as regulatory assets.

In terms of FERC hot topics, Eileen discussed FERC reporting guidance for the implementation of new accounting standards, recent FERC orders, and the recently issued FERC Enforcement Report. With respect to FERC guidance for new accounting standards implemented via a cumulative effect, she reminded participants that FERC requires approval for the use of account 439. She also discussed considerations around FERC reporting for cloud-computing costs and noted that the industry was currently discussing proposed guidance with the FERC on this topic. Regarding new FERC orders, Eileen provided a summary of FERC Order No. 864, issued on November 21, 2019. Order 864 relates to the rate-making treatment for excess accumulated deferred income taxes for electric transmission companies (applies to both formula rate companies and non-formula rate companies). Notably, the FERC has not yet issued guidance on this topic for wholesale generation or natural gas pipeline companies, so Eileen encouraged these entities to continue to monitor this for future developments. Lastly, with respect to the FERC Enforcement Report, Eileen highlighted certain cases and enforcement findings related to errors in computing AFUDC, account classification of income tax overpayments, merger transactions costs, allocated costs, and A&G expenses.
Allison Taylor discussed Hypothetical Liquidation at Book Value (HLBV) accounting. HLBV provides a methodology for allocating pre-tax GAAP income or loss to an investor when the conventional pro-rata/ownership interest does not accurately reflect the economics of the structure. HLBV calculates the amount each partner would receive if the partnership were liquidated at book value at the end of each measurement period or reporting date. The change in the allocated amount to each partner during the period is book income or loss allocated to that partner (adjusted for distributions and contributions).

There is currently no authoritative accounting guidance on HLBV. Methodology is derived from a proposed statement of position (SOP), Accounting for Investors’ Interests in Unconsolidated Real Estate Investments, dated November 21, 2000, and has been accepted in industry practice. While HLBV was established as an approach for applying equity method accounting, it has been applied by analogy to structures consolidated under the provisions of ASC 810, Consolidation, for determining allocation of earnings to noncontrolling interest holder(s).

When it comes to HLBV, it’s all in the details. The HLBV model should mirror the substance of the partnership arrangement and governing ownership documents, and the liquidation provisions of those ownership documents. Allocation percentages are typically adjusted or “flipped” once the “flip point” is achieved—the flip point occurs either through a tax equity investor achieving its target IRR (yield-based flip) or once a certain date occurs (time-based flip). The sponsor or developer often exercises a buy-out option to acquire the tax equity investor’s ownership interest during a buy-out period following the flip point being achieved.

Due to bonus depreciation and other reasons, many utilities have net operating loss carryforwards and are currently not able to utilize production tax credits (PTC) or investment tax credits (ITC). Investments made in partnerships between utilities and tax equity investors are intended to utilize credits. The key takeaway for investments in renewable assets by rate-regulated utilities is to think through implications on the revenue requirement and how such investments will be treated for ratemaking purposes.

Accounting for battery storage was discussed, including accounting matters related to battery storage agreements such as evaluating the agreements under ASC 842, Leases. The audience learned things to consider related to unit of account for battery storage agreements. The importance of understanding the arrangement, including the various services and performance obligations, was emphasized.

Allison mentioned that owners of wind energy facilities have the opportunity to repower wind farms that are past or approaching the end of their 10-year PTC period. Facilities are considered placed in service anew, restarting the 10-year PTC period, if the cost of the new property is 80 percent or more of the sum of the cost of the new property and the fair market value of the used property (“80-20 Rule”). Potential tax, valuation, and accounting issues were also discussed.
Thank you for attending the 2019 Deloitte Power & Utilities Conference. We look forward to continuing the dialogue next year.

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