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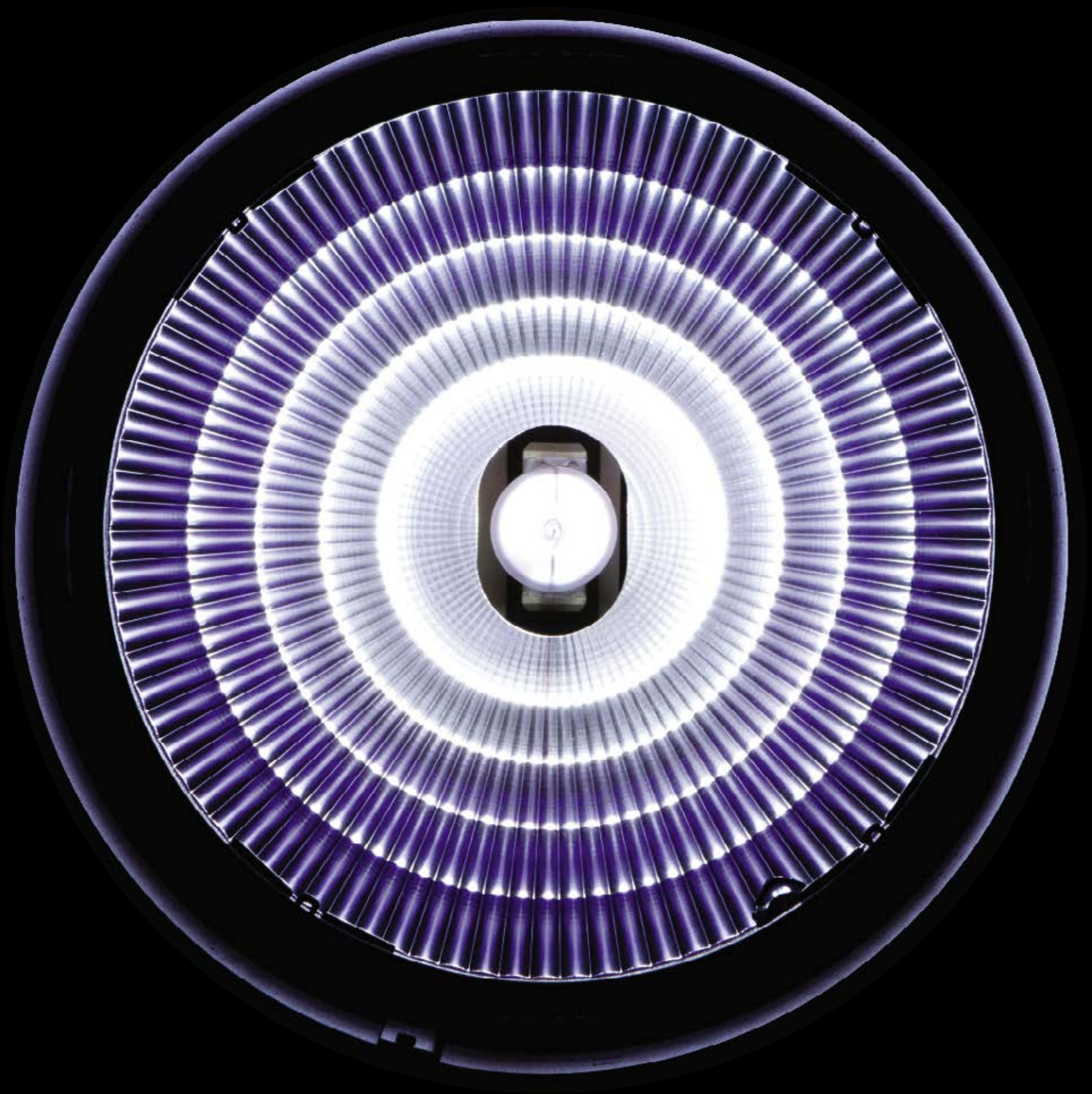


COVID-19 accounting and reporting considerations for power, utilities, and renewables

Contents

This article discusses certain industry-specific accounting and financial reporting considerations related to the COVID-19 pandemic and is organized as follows:

Introduction

The coronavirus disease 2019 (COVID-19) pandemic is affecting major economic and financial markets, and virtually all industries are facing challenges associated with the economic conditions resulting from efforts to address it. Many entities have seen sharp declines in revenues due to regulatory and organizational mandates (such as “shelter-in-place” mandates and school closures) and voluntary changes in consumer behavior (such as social distancing).

As the spread of the pandemic increases, entities are experiencing conditions often associated with a general economic downturn, including, but not limited to, financial market volatility and erosion of market value, deteriorating credit, liquidity concerns, further increases in government intervention, increasing unemployment, broad declines in consumer discretionary spending, increasing inventory levels, reductions in production because of decreased demand and supply constraints, layoffs and furloughs, and other restructuring activities. The continuation of these circumstances could have a prolonged negative impact on an entity’s financial condition and results.

The impacts of COVID-19 on the PU&R sector continue to evolve. COVID-19 is expected to impact both regulated and unregulated operations and the magnitude of the impacts will depend largely on the length and severity of the economic downturn experienced in impacted regions. Operational disruptions may occur in a number of areas, including generation operations, grid reliability and mutual assistance networks. Supply chain issues impacting critical parts for new construction as well as plant maintenance are also possible. Governmental policy directives in response to the outbreak will also need to be carefully considered. In certain markets, such directives may directly impact local utility providers as governments attempt to provide financial relief to citizens through measures which could include reduced utility bills. In addition, most utilities in the United States have suspended service disconnections for non-payment either voluntarily or in response to state mandate.

For broader accounting and financial reporting considerations related to conditions that may result from the COVID-19 pandemic, please refer to Financial Reporting Alert 20-2, *Financial Reporting Considerations Related to COVID-19 and an Economic Downturn* (FRA 20-2), issued on March 25, 2020.

Accounting considerations

Impairment considerations

Goodwill and other intangible assets

In accordance with ASC 350, goodwill of a reporting unit should be tested for impairment on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. Historically, declines in the stock market can trigger testing of goodwill and other intangible assets for impairment. However, other factors (triggers) that may accompany stock price declines are typically examined as well. These include:

- Financial triggers: Market volatility, credit risk, commodity risk
- Operational triggers: Facility closures, decreased demand, reduced human capital
- Strategic and reputational triggers: Competitive shifts, technology innovation, industry convergence
- Geopolitical and regulatory triggers: Health pandemic, trade disruptors, sustainability risks
- Extended enterprise triggers: Supply chain interruptions, distribution delays, reliance on third parties

Specific to the pandemic, potential triggers for PU&R entities could include:

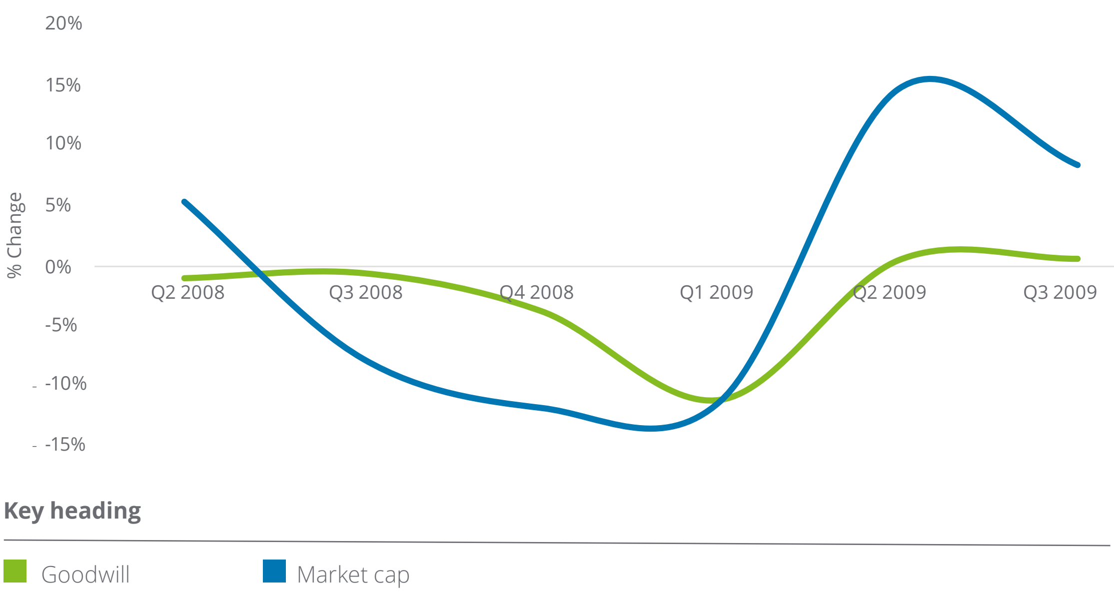
- *Impacts to demand* – There is potential impact on power and natural gas consumption as a result of certain shelter-in-place orders throughout the nation. Commercial and industrial demand can be impacted by pandemic-related closures and adjusted operating hours of nonessential businesses. Concerts, sporting events, and conferences are being cancelled or deferred, which can further impact demand in the short term. In contrast, residential consumption is generally increasing as shelter-in-place orders continue. The impact to demand can fluctuate entity by entity based on the geography and the related shelter-in-place orders for the relevant regions. Additionally, the mix of customer classes can have an impact on the demand. There is a level of uncertainty as it relates to the impacts to demand, given the open-ended and uncertain duration of shelter-in-place orders. Even when shelter-in-place orders end, there could be continued impacts to demand due to impacts of an economic downturn.
- *Supply chain interruptions* – Entities with projects under construction should consider the impacts of supply chain interruptions. Supply chain issues can impact both residential and large-scale project timelines. To the extent construction is heavily reliant on materials from foreign and domestic geographies that are significantly impacted by the pandemic, entities should consider the possibility of delays in procuring those materials and the related impact to construction timelines. Supply chain interruptions increase project execution risk. If there are significant impacts to the planned construction timeline, entities should consider whether this results in a triggering event.
- *Workforce disruptions* – Similar to supply chain interruptions, disruptions in the workforce should be assessed for the impact on the operating needs of the business, particularly in those instances where a physical presence is required, such as construction activities, operation and maintenance of a power plant,

or responding to potential gas leaks. While a portion of the workforce may be considered critical to the operation of the business and the delivery of electricity and gas to consumers, there are risks related to the pandemic for the availability of the workforce, whether that be the result of illness or shelter-in-place orders for certain regions.

Entities should consider whether the economic downturn combined with one or more of the above triggers results in the need for an impairment test during the interim period. For the period January 1, 2020 to March 31, 2020, the S&P 500 Index declined 21 percent and the S&P 500 Utilities Index declined 13 percent.[1] Consideration of the economic downturn is particularly important for those reporting units with recent transactions resulting in significant goodwill or those reporting units with only a small excess of fair value over carrying amount at the time of its most recent quantitative test, especially if a reporting unit may have been discussed in prior disclosures related to goodwill of reporting units as higher risk for impairment.

The 2008 Financial Crisis provides a guidepost to how companies viewed impairment testing during periods of market volatility. The below analysis shows that the impairments recognized by public utilities and independent power producers tracked closely with decreases in their market capitalization.

Figure 1. Power and utilities market cap declines and goodwill impairment



Source: S&P Capital IQ.
Population: Public utilities and independent power producers—traded as of January 2008.

Long-lived assets

In accordance with ASC 360, when events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable, the utility should conduct a review for impairment. In determining the grouping for long-lived assets, an entity should determine the level at which assets are grouped on the basis of the entity's facts and circumstances. For many rate-regulated utilities, the asset group is very large because the revenues from regulated customers cannot be identified with respect to any subset of assets. Accordingly, many utilities have concluded that the lowest level of identifiable cash flows is related to the entire rate base for a rate jurisdiction, or perhaps a subset such as the regulated generating fleet if the customer bill has a separately identified component for the power cost. By contrast, unregulated

1. Analysis prepared utilizing prices from January 1, 2020 to March 31, 2020 obtained from S&P Global Market Intelligence.

power plant businesses may be able to identify cash flows at a lower level than the entire generating fleet, such as by region or individual plant. Examples of events and circumstances that indicate that the carrying amount of an asset or asset group may not be recoverable (triggers) include:A significant decrease in the market value

- A significant adverse change in the extent or manner of use or significant physical damage
- A significant adverse change in legal factors or business climate, including an adverse action or assessment of a regulator
- An accumulation of costs significantly in excess of the amount originally expected
- A current-period operating or cash flow loss combined with a history of losses or a forecast of continuing losses
- A current expectation, more likely than not, that a sale or other disposition will occur significantly before the previously estimated useful life or lives

The above are not the only triggers that indicate a potential impairment of long-lived assets. Significant changes in the regulatory environment or losses of major customers that result in stranded costs are also events that would indicate that a utility should review its assets for impairment.

The impacts of the pandemic should be considered to determine whether they indicate the carrying amount of an asset or asset group may not be recoverable. As it relates to long-lived assets, entities should consider the same potential triggers discussed for goodwill and intangible assets above (impacts to demand, supply chain interruptions, and workforce disruptions). Entities will need to consider whether there is: (1) a decline in revenues, (2) an increase in costs, or (3) a combination of both as a result of the pandemic. These changes may indicate a decline in net cash flows, which may indicate the need to test long-lived assets for recoverability. The risk of impairment for unregulated assets could be higher, depending on the impacts of the pandemic on each entity. With the current economic environment, the need to evaluate for impairment of long-lived assets could become increasingly frequent.

Specifically, as it relates to impacts of the pandemic, PU&R entities should consider:

- *Renewable projects under construction* – Construction timelines in the renewable energy sector are under pressure due to shelter-in-place orders in various states and because of supply chain interruptions in China and elsewhere. Foreign markets produce many of the components used in wind and solar generation facilities. In some cases, these interruptions could jeopardize a developer's ability to complete construction in time to qualify for federal tax credits. Often, the tax credits are necessary to make the project economically viable, and some developers will have to face difficult decisions about completing construction or abandoning the project.
- *Capitalized development costs* – There are also impairment considerations for projects that have not yet commenced construction but where an entity has capitalized development costs. For example, development pipelines could be affected by the scarcity of available financing. In the United States, failure to obtain financing and begin construction by the end of 2020 will jeopardize a project's eligibility for tax credits unless the federal government extends the deadline or offers targeted relief to lessen the impact of COVID-19. As mentioned above, tax credits may be necessary to make a project economically viable, which could lead to decisions regarding whether the project should be abandoned.
- *Midstream* – The reduction in prices for oil in the first quarter of 2020, and to some extent natural gas, may impact expected future throughput volumes and cash flows and could therefore be a change in circumstance for an asset group that may require the asset group to be tested for impairment
- *Merchant power* – Entities with merchant power plants should evaluate if the expected impacts to demand or other impacts of an economic downturn, including the impacts on forward power prices and capacity prices,

could be an event or change in circumstance that would indicate the carrying value of the merchant power plant or the merchant power asset group may not be recoverable.

Entities should consider whether these circumstances represent a trigger, which would result in the need to test the assets or the capitalized development costs for impairment. There may also be disclosure considerations, including concentration risk with respect to supply chain issues and the risk associated with meeting the tax credit deadlines.

For more information on the tax credit considerations in the current environment see the Tax considerations section.

Regulatory assets

As with most companies, utilities are likely incurring or anticipating incremental costs associated with their crisis management and pandemic response, including, but not limited to:

- Incremental bad debts as a result of the moratoriums set by many states on utility disconnects for nonpayment
- Incremental labor costs, such as overtime, that would not be incurred during the normal course of business
- Costs associated with the establishment of temporary customer service centers
- Redundant workforce costs to cross-train employees in the event employees become ill
- Additional sanitation and cleaning costs for offices, facilities, plants, and vehicles
- Cost of personal protective equipment necessary for essential employees
- Incremental technology costs incurred to allow employees to work remotely

Many rate-regulated entities are currently evaluating if these incremental costs meet the criteria in ASC 980 for deferral as a regulatory asset. ASC 980-340-25-1 states that the "rate actions of a regulator can provide reasonable assurance of the existence of an asset." All or part of an incurred cost that would otherwise be charged to expense should be capitalized as a regulatory asset if:

- It is probable that future revenues in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes; and
- Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred cost rather than to provide for expected levels of similar future costs.

An incurred cost is defined in ASC 980-10 as "a cost arising from cash paid out or obligation to pay for an acquired asset or service, a loss from any cause that has been sustained and has been or must be paid for," while probable is defined in ASC 450-20, *Contingencies – Loss Contingencies* as "likely to occur."

Evidence that a regulatory asset is probable of recovery is a matter of professional judgment based on the facts and circumstances of each case. Utility management's positive representation that each regulatory asset is probable of recovery in future rates is required. As a reminder, evidence that could support future recovery and corroborates utility management's representation includes:

- Rate orders from the regulator specifically authorizing recovery of the costs in rates
- Previous rate orders from the regulator allowing recovery for substantially similar costs
- Written approval from the regulator approving future recovery in rates
- Analysis of recoverability from internal or external legal counsel

The best evidence of a regulatory asset is a rate order. However, to the extent that regulatory commissions and their staff are subject to home sheltering or are deemed nonessential services in harder-hit geographies, the flow of regulatory communication and action will likely slow. In other jurisdictions, proceedings have already begun to consider the recovery of costs. While it is likely there is no precedent for recovery of pandemic costs and the ability to discuss the possible outcomes with regulatory commissions may be limited, an analogy in many jurisdictions could be storm cost recoveries, as they represent significant and unexpected costs incurred outside the control of the company in connection with a crisis situation. It is important to remember each case and regulatory jurisdiction will be different, and the assertion that costs are probable of recovery will require a significant amount of judgment. Consultation with entities' regulatory and legal counsel may be appropriate to assist in this judgment.

For most calendar-year entities located within the United States, significant costs may not yet have been incurred as of the end of the first quarter related to COVID-19, given the timing of the domestic impacts of the pandemic. While incurred costs may not yet be significant, entities should consider tracking costs, given the uncertainty of the full impacts of the pandemic. Under guidance included in ASC 980-340-25-1, an incurred cost that does not meet the asset recognition criteria at the date the cost is incurred should still be recognized as a regulatory asset when it meets those criteria at a later date. Therefore, a lag in regulatory action will not preclude an entity from recognizing a regulatory asset in future periods.

Beyond cost deferrals, many rate-regulated utilities and regulators are evaluating or in some cases are in active discussion regarding the potential for recovery of lost revenues due to the significant reduction in demand or the voluntary or mandated suspension of other customer billings. In a few cases, regulators have issued orders that specify how lost revenue amounts will be determined and billed to customers. In other cases, regulators have indicated support for allowing the recovery of lost revenues, but specifics of how lost revenues will be determined and billed in the future will be the subject of further proceedings. Questions have arisen regarding the GAAP accounting for lost revenue amounts that may be billable in the future. The accounting guidelines for recording revenue or profit as a regulatory asset are more strict than the accounting guidelines for recording incurred costs as a regulatory asset. ASC 980-605 provides guidance for alternative revenue programs that allow rate-regulated utilities to bill customers for certain incremental revenue amounts in future periods but are associated with prior activities. Under the guidance, a regulated utility shall recognize additional revenues if **all** of the following conditions are met:

1. The program is established by an order from the utility's regulatory commission that allows for automatic adjustment of future rates. Verification of the adjustment to future rates by the regulator would not preclude the adjustment from being considered automatic.
2. The amount of additional revenues for the period is objectively determinable and is probable of recovery.
3. The additional revenues will be collected within 24 months following the end of the annual period in which they are recognized.

These conditions are not to be used as guidelines; rather, they set a high hurdle for recognizing revenue under an alternative revenue program, and all of these conditions must be met. This guidance is limited to rate-regulated utilities under ASC 980 and, as noted above, to situations in which future rates would be adjusted to provide additional revenue "in response to past activities or completed events." To the extent that a utility does not have an existing program that addresses the conditions in ASC 980-605 (such as a decoupling mechanism), determining whether a regulatory directive or order to defer lost revenues in response to COVID-19 qualifies as an alternative revenue program in which revenue can be recorded currently will depend on the specific facts and circumstances of each situation and will require significant judgment. Further, for orders from a regulator that deal with recovery of lost revenues that are received after the balance sheet date, but before the financial statements are issued, careful evaluation of the subsequent events literature under ASC 855 will be required to determine if such events represent conditions that existed at the balance sheet date requiring adjustment to or accrual in the financial statements, or disclosure with impacts recorded in the subsequent period.

In certain circumstances, regulators may also authorize the utility to record a carrying cost on deferrals at the utility's authorized weighted average cost of capital, which includes the capital cost of both equity and debt. As a reminder, other than the accrual of AFUDC on construction work in progress or the equity return embedded in revenue under a qualifying alternative revenue program subject to ASC 980-605 discussed above, the deferral of an equity return is prohibited under ASC 980-340-25-5, which states that "an allowance for earnings on shareholders' investment is not an incurred cost that would otherwise be charged to expense. Accordingly, such an allowance shall not be capitalized pursuant to that paragraph."

Lastly, to the extent that rate regulation is included as a critical accounting estimate in the MD&A, companies should consider the necessity of including disclosure of any significant pandemic-related regulatory assets recorded or significant costs incurred that may meet the criteria of a regulatory asset in a future period, given the significant management judgment involved. Such disclosures would include considerations around the probability of recovery in future rates and the information considered in evaluating whether it is appropriate to record a regulatory asset.

Impact of government policy initiatives on customer billing practices

Customer accounts receivable are generally reported net of a provision for uncollectible accounts. Certain segments of a utility customer base may experience employment layoffs or other displacements related to COVID-19, which may negatively affect the customers' ability to pay utility bills on a timely basis. This could result in a short-term phenomenon of "slow-pays and no-pays" as customers react to the current environment. In addition, many utilities have either volunteered or been ordered to cease all service shutoffs for nonpayment during the pandemic, and some entities may ultimately be subject to other types of payment abatement programs imposed by regulators or local governments. As a result, it will be important for utilities to carefully consider what credit losses to expect in the current environment. When evaluating the payment it expects to receive from customers, an entity should consider issues associated with a customers' ability to pay, as well as the entity's payment accommodations. For some utilities, any incremental bad debt expenses that arise from the current circumstances may be recoverable in future rates; in such cases, the entity should consider whether a regulatory asset should be recorded for these costs. Refer to the regulatory assets discussion within this section for more information.

Given the requirement to assess collectability in applying the revenue framework in ASC 606, some companies have asked about the impact of service shutoff moratoriums on revenue recognition practices. Specifically, companies have inquired about any required changes to revenue recognition practices for customers that may have a higher risk of nonpayment. The voluntary and governmental policy actions in response to COVID-19 directly affect many of the credit mitigation techniques that utilities have historically relied upon in supporting collectability. Accordingly, it is important to address that impact, as well as whether and to what extent other methods for recognizing revenue in this situation for certain customer groups may be necessary. Such methods may include cash basis revenue recognition or delayed recognition whereby consideration received is reported as a liability (because additional service must continue to be provided without the ability to disconnect).

The impact of this issue may be greater for those that do not have the ability to recover bad debts through rates. As of the date of this publication, we are considering this question and working closely with others in the industry in evaluating the accounting requirements. For companies that are impacted by this issue, we recommend consultation with your auditor

For more information on the impact of COVID-19 on critical accounting estimates in MD&A, refer to the SEC reporting and disclosure considerations section.

or accounting adviser. In many cases, the financial impact on the first quarter may not be material for many companies given the timing of the pandemic responses, which in many jurisdictions were implemented in March 2020.

Deferral of CECL not extended beyond insured depository institutions and credit unions

The FASB's current expected credit losses standard ("CECL") is effective for most public companies for fiscal years beginning after December 15, 2019. Section 4014 of the CARES Act offers optional temporary relief from applying CECL only for insured depository institutions and credit unions.

After the issuance of the CARES Act, there was some speculation that a broader deferral of CECL may be considered by the FASB and/or the SEC. However, on the basis of discussions with the SEC staff, we understand that the SEC would object to the application of the CARES Act's provisions by an entity that is not eligible to apply them. In other words, the optional deferral of CECL under Section 4014 of the CARES Act is limited to insured depository institutions and credit unions.

Pension accounting considerations

Many entities within the PU&R sector have significant defined benefit plan obligations. These entities may be considering whether a significant decline in the value of plan assets and other economic uncertainties resulting from the pandemic would require interim remeasurement of a defined benefit plan prior to the required year-end remeasurement. Under ASC 715, a significant decline in the fair value of plan assets as a result of market declines does not represent a significant event that would call for an interim remeasurement of defined benefit plan assets and obligations. Although entities may not need to perform an interim remeasurement, disclosures in the interim financial statements may be required, particularly for entities that may anticipate recognition of significant actuarial losses associated with unrealized losses on plans assets at the end of the year—especially those entities that recognize actuarial gains and losses immediately in the income statement.

Further, while COVID-19 and the related market declines do not result in a required interim remeasurement, other matters unrelated to the pandemic or indirectly related to the pandemic may result in a remeasurement of a defined benefit plan obligation during this time period. Examples of such significant events include:

- Plan amendments
- Settlements or curtailments
- Business combinations
- Plan mergers and split-ups

For example, some entities may have pension plans that permit employees to elect to receive their pension benefit in a lump sum, which could result in multiple lump-sum payments over the course of the year. Under the guidance in ASC 715-30-35, when settlements occur in an interim period during a year in which it is probable that the cumulative settlements for the year are expected to exceed the service-cost-plus-interest-cost threshold, an entity should assess whether it is probable that the criteria for settlement accounting will be met (for example, whether the total settlements will exceed the threshold). If the entity concludes it is probable that the threshold will be exceeded during the year, the entity should apply settlement accounting on at least a quarterly basis rather than wait for the threshold to be exceeded on a year-to-date basis. Accordingly, the entity should complete a full remeasurement of its pension obligations and plan assets in accordance with ASC 715-30-35. Upon remeasurement, an entity should adjust its statement of financial position in a subsequent interim period to reflect the overfunded or underfunded status of the plan consistent with that remeasurement date. Given the recent turbulence in the stock market and other economic uncertainties, the determination of the fair value of plan assets, as well as the selection of the appropriate discount rate to apply, will likely be more challenging and require significant judgment. For matters to consider when performing a remeasurement of a defined benefit plan and for other COVID-19 impacts on the accounting for defined benefit plans, stock compensation plans and employee termination benefits, please refer to FRA 20-2.

Tax considerations

Impact of supply chain disruption on construction timelines

Construction timelines in the renewable energy sector are under pressure due to shelter-in-place orders in various states and supply chain disruptions in China and elsewhere. Foreign markets produce many of the components used in wind and solar generation facilities. Such disruptions could affect both residential applications and large-scale projects. In some cases, these disruptions could jeopardize a developer's ability to complete construction in time to qualify for federal tax credits. Often, the tax credits are necessary to make the project economically viable, and some developers and investors will have to face difficult decisions about completing construction or abandoning the project. In other cases, development pipelines will be affected by the scarcity of available financing. In the United States, failure to obtain financing and begin construction by the end of 2020 will jeopardize a project's eligibility for certain tax credits unless the federal government extends the deadline or offers targeted relief to lessen the impact of COVID-19.

Companies recording interim period tax provisions based on a projected annual effective tax rate (AETR) that have historically included credits for facilities expected to be placed in service later in the year should consider the impact of a postponed placed-in-service date on the amount of production tax credit (PTC) or investment tax credit (ITC) expected to be recognized in 2020 on the projected AETR used in computing the tax provision for the first quarter of 2020.

We expect that additional federal stimulus legislation, including income tax incentives and relief, will be enacted in 2020. Proposals under consideration include relief from the requirement to show continuous progress of a project with respect to the "begun construction rules." These rules determine the amount of PTC or ITC available for a renewable energy facility that began construction before one of the dates prescribed in the statute during the multiyear phase-down of PTC and ITC rates. Under existing law, a facility is deemed to satisfy the continuity requirement if it is placed into service by the end of the fourth tax year after construction begins. One proposal is to extend this four-year safe harbor to a six-year safe harbor.

Another proposal would allow companies to elect to treat the PTC and ITC as refundable credits. In general, refundable credits are not reported as income taxes. Instead, the benefits are recorded as reductions of pretax costs (similar to accounting for grants). Investment-based refundable credits are recognized over the life of the investment. Immediate recognition under a flow-through approach is not available. These rules also apply to tax credits that are refundable based on taxpayer election even if the taxpayer does not elect the refundable option unless there is a significant economic disadvantage to electing to convert the credit to a refundable credit. The evaluation of the economic impact of electing to convert to a refundable credit may be an entity-specific evaluation and would include a consideration of state taxation.

Taxpayers may also seek relief in the form of regulatory or administrative guidance from the IRS and Treasury to ease some of the requirements of PTC and ITC qualification as a result of these supply chain and construction delays.

Bad debt reserves

As discussed in the Accounting considerations section under **Impact of government policy initiatives on customer billing practices**, COVID-19 is expected to negatively affect certain customers' ability to pay utility bills on a timely basis, resulting in a short-term phenomenon of "slow-pays and no-pays." In addition, new restrictions on service shutoffs (whether voluntary or required) will expose utilities to increased credit losses which may or may not ultimately be recoverable through rates.

The changes in billing and collection practices may result in increases in bad debt reserves and the timing of write-offs of accounts receivable. The timing of write-offs is critical in determining the timing of tax deductions for wholly or partially worthless debts. Increases in bad debt reserves will generally result in a temporary difference when applying the rules for accounting for income taxes. For companies that "flow through" the tax effects of this temporary difference as a result of the periods in which the regulator provides for recovery of income tax costs in establishing rates, the changes in collection practices may result in a more significant impact than usual on the effective income tax rate, including the projected AETR used for interim period tax provisions.

CARES Act – Five-year net operating loss carryback

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) was enacted on March 27, 2020, and includes modifications to the net operating loss (NOL) limitation and carryback rules. The CARES Act provides for a five-year carryback for NOLs arising in taxable years beginning in 2018, 2019, and 2020. The CARES Act also provides for a temporary removal of the 80 percent limitation on NOL utilization for taxable years beginning before January 1, 2021.

A carryback of an NOL to 2013–2017 tax years is significant, in part, due to a higher corporate income tax rate (35 percent) applying in the carryback year than in the loss year (21 percent). Thus, a permanent tax savings lowering the effective income tax rate results. Entities that will now be able to carry back NOLs to prior years or utilize more NOLs in the current and/or prior years as a result of the CARES Act should consider the impact of these tax law changes on their income tax payable and receivable, projected AETR used for interim period tax reporting, deferred tax assets, and associated valuation allowance, if any. The effects of a change in tax law on a deferred tax liability or asset (and related valuation allowance) are included in continuing operations and recognized in the period of enactment (that is, not apportioned among interim periods through an adjustment of the projected AETR).

A regulated utility will need to assess whether any permanent tax benefit resulting from carryback to a tax year with a higher tax rate should be recorded as a tax benefit in the income statement or as a regulatory liability. The CARES Act does not include a normalization requirement to "protect" this tax benefit or to prescribe a time and manner to share the benefit through regulated rates. Utilities will need to assess a variety of factors, including potentially the ratemaking treatment of incremental pandemic-related costs, in judging whether it is probable that some or all of such tax benefit will be used to lower future customer rates.

Interim period tax provisions

Accounting rules for determining interim income tax expense include the use of the projected AETR to determine interim period tax provisions. The uncertainties regarding forecasting pretax book income for 2020 and certain permanent book-tax differences and credits for this period present unique challenges for first-quarter reporting. Further, as described above, certain tax items must be recorded in full in the financial reporting period in which the transaction, change in tax law, or change in judgment occur. Companies should consider whether expanding the description of their accounting policy for interim period tax provisions would be useful to help readers understand variances between 2020 tax amounts and effective income tax rates and amounts and rates for prior periods, or for purposes of explaining a significant estimate reflected in the financial statements.

Employee retention credit

The CARES Act also created a COVID-19 employee retention tax credit (CRC) of up to $5,000 per eligible employee. Eligible employers are taxpayers experiencing either (1) a full or partial suspension of business operations stemming from a government COVID-19-related order, or (2) a more than 50 percent decrease in gross receipts compared to the corresponding calendar quarter in 2019. This 50 percent credit applies to up to $10,000 in qualified wages paid during the period beginning March 13, 2020, and ending on December 31, 2020, and is refundable to the extent it exceeds the employer portion of payroll tax liability. Because the CRC is a payroll tax credit, tax-exempt entities are also eligible to claim it.

Eligible wages or employer-paid health benefits must be paid for the period of time during which an employee did not provide services. However, employees need not stop providing all services to the employer for the credit to potentially apply.

Though these benefits are not related to income tax liabilities, companies with book-tax differences for payroll taxes, perhaps related to the capitalization of costs related to self-constructed property, should consider these credits in estimating book-tax basis differences.

SEC reporting and disclosure considerations

For further information regarding these items, among other accounting and disclosure considerations, refer to FRA 20-2

The SEC expects registrants to clearly disclose material risks and uncertainties. As a result, most entities will need to disclose the impact of COVID-19 in various sections of their SEC filings, including the risk factors section, MD&A, the business section, legal proceedings, disclosure controls and procedures, internal control over financial reporting, and financial statements. In DG Topic 9 (issued March 25, 2020), and in a manner consistent with other guidance on evolving risks, the SEC staff provided a series of illustrative questions for registrants to consider when developing disclosures related to the current and expected future impact of COVID-19. Additionally, on April 8, 2020, the SEC released a public statement reinforcing the importance of disclosure for investors, markets, and the fight against COVID-19.

The following discussion focuses on risk factors and MD&A and includes certain disclosure considerations specific to PU&R. Registrants should tailor disclosures to be specific to their own facts and circumstances. In addition to the items discussed below, registrants should be mindful of disclosures related to non-GAAP measures and key performance indicators (KPIs), as well as information included in earnings releases. For further information regarding these items, among other accounting and disclosure considerations, refer to FRA 20-2.

Risk factors

Registrants must disclose information about the most significant risks facing the entity or its securities. Historically, a company's risk factors have often been fairly consistent from period to period, but the significant and rapidly evolving impact of COVID-19 could result in the need for more frequent (and more significant) updates. For example, while many registrants may already disclose their general risk related to issues such as potential natural disasters or pandemics, they should consider whether to update the disclosure to clarify that the risk is no longer hypothetical and to provide more specificity about the actual and potential future impact of COVID-19. Within PU&R, relevant concepts that may be considered in a registrant's risk factors may include, but are not limited to, the following:

- Risks related to the impact on current and future ratemaking (for example, potential impact on true-up mechanisms and the related impact on regulatory assets and liabilities).
- Risks related to a registrant's ability to access capital markets due to the economic downturn.
- Risks resulting from decreased routine maintenance (for example, reduced tree trimming) and/or capital investment and the related regulatory impact (for example, new plant construction that has ceased).
- Risks related to government-imposed moratoriums on service disconnections and other required changes to billing practices.

- Risks to supply chain due to decreased production and imports of materials and supplies.
- Risks related to short-term and long-term impacts of grid operations and protocols for mutual assistance.
- Steps the registrant has taken to date to mitigate applicable risks.

In the weeks of March 23 and 30, 2020, there were more than a dozen industry-launched offerings for the issuance of debt securities. Substantially, all of these offerings included one or more risk factors in the prospectus supplement that referred to COVID-19.

MD&A

MD&A supplements the financial statements by providing information about a registrant's financial condition, results of operations, and liquidity. A registrant should discuss in its MD&A the material quantitative and qualitative impact of COVID-19 on its business. For example, the discussion could address potential issues such as changes in consumer behavior, including an unusual increase or decrease in demand, increased competition for raw materials, supply chain interruptions, commodity price disruption, risk of loss on significant contracts, liquidity challenges or debt covenant issues, regulatory risks, or the impact on human capital.

Results of operations

SEC Regulation S-K, Item 303 requires disclosure of "significant economic changes that materially affected the amount of reported income from continuing operations and, in each case, indicate the extent to which income was so affected." Registrants in PU&R should ensure that the discussion in results of operations sufficiently characterizes the key drivers causing reported variances and quantify those items that have a material impact on operating results, with specific discussion of the impacts of COVID-19. Examples include, but are not limited to, the following:

- Decreased commercial and industrial volumes and increased residential volumes.
- Volatility in cost of sales due to changes in commodity prices.
- Changes in operating expenses due to reduced routine maintenance or increased pandemic-related costs.
- Volatility in interest expense as the market responds to COVID-19 (for example, impact on floating-rate debt).
- Impact of the CARES Act. See Tax considerations section for further discussion of the CARES Act.

Liquidity and capital resources

As a result of the COVID-19 pandemic, liquidity may be significantly affected given the potential disruptions to normal levels of revenues and operating cash flows, as well as to access to cash through debt or equity markets. In their MD&A disclosures about liquidity, registrants should consider discussing their working capital or other cash flow needs, anticipated changes in the amount and timing of cash generated from operations, the availability of other sources of cash along with potential limitations associated with accessing such sources, and the possible ramifications of their inability to meet their short- or long-term liquidity needs.

In addition to discussing the impact on historical results, registrants are also expected to disclose, in accordance with SEC Regulation S-K, Item 303, "any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact" on their financial condition, results of operations, or liquidity. For example, as discussed in the Accounting considerations section, some registrants may be at risk for significant goodwill impairments, or the recoverability of certain regulatory assets may be uncertain. These forward-looking disclosures are especially critical in connection with events such as the COVID-19 pandemic and the related economic uncertainty. Such disclosures can give investors an "early warning" about risks such as (1) when and under what conditions charges may be incurred in the future and the potential magnitude of such charges, (2) when revenue growth or profit margins may not be sustainable because of underlying economic conditions, or (3) when the registrant may be unable to comply with debt covenants or have other liquidity issues.

Critical accounting estimates

The SEC's interpretive guidance[2] states that critical accounting estimate disclosures should "supplement, but not duplicate, the description of accounting policies in the notes to the financial statements and provide greater insight into the quality and variability of information regarding financial condition and operating performance." Given the uncertainty associated with COVID-19, there is likely to be a substantial increase in the level of judgment entities need to apply in estimating future results and the potential range of reasonably likely outcomes. Registrants should therefore consider expanding their disclosures about (1) the key assumptions used in their most significant estimates and (2) the sensitivity of such estimates to changes that could reasonably occur as events associated with COVID-19 continue to develop. Certain critical accounting estimates that could be significantly impacted in PU&R include, but may not be limited to, collectability of customer receivables, recoverability of regulatory assets, impairment risk of goodwill and long-lived assets, valuation of pension assets and liabilities, and contingent liabilities.

Consequently, registrants should consider updating, in their quarterly report on Form 10-Q, the critical accounting estimates previously disclosed in the Form 10-K to the extent that there have been material changes to key assumptions and estimates or a significantly increased likelihood of charges in future periods due to the high variability of estimates in the current environment.

MD&A disclosures are typically included in a Form 10-K or Form 10-Q, but due to the rapidly evolving impact of COVID-19, registrants may also file current reports on Form 8-K to update investors on the current and potential future impact of COVID-19 on their business. Many of these filings have also announced that registrants are withdrawing or updating previously issued guidance related to expected 2020 revenue and earnings targets.

2. See Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations, SEC Release No. 33-8350; 34-48960; FR-72 (December 29, 2003), available at https://www.sec.gov/rules/interp/33-8350.htm

ICFR considerations

Internal control over financial reporting

The impact of COVID-19 has resulted in a number of considerations regarding internal controls, including the need to implement new controls or to modify existing ones. Entities must disclose in their quarterly or annual filings any changes in internal controls that have materially affected, or are reasonably likely to materially affect, their ICFR in Item 4 of Form 10-Q or in Item 9A of Form 10-K (or in Item 15 of Form 20-F for foreign private issuers).

Entities will need to consider the operating effectiveness of controls, including assessing any breakdown in review-type controls or the inability of individuals to perform control duties because of absences (for example, because of employee illness or the closure of affected locations). Entities should also consider how a lack of information may affect management's ability to effectively operate controls (for example, personnel may not be available in affected areas to provide information that is essential to the effective operation of an internal control). If an existing control cannot be performed, management may need to identify alternative appropriately designed controls to compensate for the lack of information, as well as to potentially identify and evaluate control deficiencies.

Some specific considerations related to internal controls for PU&R entities may include, but are not limited to, the following:

Revenue

- *Customer service centers* – Utilities use service centers as an entry point in supporting customer interaction, collaborating on billing tasks, and processing revenue. Due to the social distancing guidelines, customer service representatives may now be working remotely while performing functions within the customer information system. Also, certain employees may require additional access in the system if job responsibilities are modified in order to provide coverage. These employees perform critical revenue cycle controls such as reviewing customer bill exceptions, reviewing collectability, and performing adjustments to bills. Without appropriate supervision, employees may consider work-arounds to existing procedures or controls. Further, the inability to meet live and conduct discussions with revenue supervisors may impact the design or operation of these business cycle controls. Extra scrutiny should be placed on segregation of duties considerations and access reviews if employees are provided additional system access. Utilities should also consider any temporary modification to revenue review controls (for instance, electronic evidence to support bill adjustments) and enhance activity monitoring of account adjustments. Additionally, some entities have outsourced the customer call centers to third parties, including those in other countries. The customer service representatives in some offshore call centers may not have the infrastructure to work remotely, which in turn has substantially increased the burden on the domestic call centers at some entities. Entities should evaluate the impact on the operating effectiveness of controls in situations when employees have very high workloads for extended periods.

- *Meter-reading* – While a number of utilities have moved to advanced metering infrastructure (AMI) processes, some companies lacking these devices will be impacted by the new social distancing guidelines. Meter-readers may be unable to visit a premise to perform readings. This would result in the utility having to estimate energy usage and consumption, which could prove challenging given the fluctuations with new working arrangements and usage patterns. Utilities should consider the appropriateness of their billing estimation controls and whether they align with the anticipated changes in customer usage.

- *Billing validation checks* – Utilities use automation within their customer information systems to identify potential reading and billing exceptions through validation routines. These validations include formulas using thresholds and comparisons of prior usage to expectations for current usage. COVID-19 creates potential changes to energy usage, such as a spike in residential and decline in commercial and industrial usage. Utilities should consider revisiting the criteria for investigation (automated configurations) to ensure that these usage variations are appropriately captured and accounts requiring manual resolution are appropriately investigated and adjusted.

Regional transmission organizations (RTOs) and Independent system operators (ISOs)

- Utilities often rely on their RTOs and ISOs to coordinate, control, and monitor the grid. These external organizations provide information regarding energy revenue and cost that is essential to the control environment. Utilities must ensure that transactions with ISOs and RTOs are accurately recorded, especially given the current volatility in energy usage and prices. Additionally, settlement review controls will now be performed by employees working remotely. Control owners must have access to sufficient documentation (power purchase agreements, bank statements, invoices, and disbursements) to review and approve the appropriateness of the transactions. Entities should consider any modifications to controls to ensure the reliability and availability of the information. For example, entities may need to utilize electronic evidence to replace any hard copies.

Property, plant, and equipment (PP&E)

- As COVID-19 causes alternative working conditions with only essential work being performed, previous assumptions used to develop construction work in progress estimates may no longer be appropriate in the current environment. Additionally, the reassessment of project timelines and work order completion may require further analysis of PP&E account balance classification. Utilities should consider any modifications needed for internal controls over the estimation of cost activities to ensure they are being accurately recorded in the correct time period and to determine whether the balances are reasonable.

Inventory

- Utilities use materials and supply inventory and equipment for the maintenance of the grid and construction of new infrastructure projects. As COVID-19 has created global supply chain disruptions and interruptions, utilities have been affected by both the availability and valuation of inventory. In many cases, warehouses are working with skeleton crews and workers have been forced to stay home due to social distancing guidelines. Utilities should consider any modifications to inventory count and valuation controls, as well as ensuring that proper segregation of duties is maintained between plant personnel receiving the inventory and approvers to prevent inventory shrinkage.

General information technology (IT) controls

- Like all companies, utilities rely on an effective IT control environment to support operations and financial reporting. With increased dependency on IT personnel and infrastructure to support the organization working remotely, the availability of IT personnel for internal control–related matters could be limited. Additionally, utilities must plan for increased levels of remote system access and remote user acceptance testing (UAT) for system implementations. Risks around cybersecurity are likely to be heightened during the pandemic and some companies may need to strengthen controls to prevent remote workers from compromising company data. Utilities should consider preemptive reviews on monitoring and contingency plans for IT personnel and projects so that key controls can continue to be operated and segregation of duties enforced.

Financial close and reporting

- Entities should also consider management's ability to complete its financial reporting process and prepare its financial statements on a timely basis. Delays in closing the underlying financial records may increase the potential for error in the financial statements and merit the use of new or modified controls. In addition, entities will need to ensure that they have properly designed and implemented controls related to the selection and application of GAAP for the accounting and disclosure issues arising from the COVID-19 pandemic. As noted above in Accounting considerations, the accounting and reporting for many of the issues arising from the pandemic involve complex or especially subjective management judgments and estimates, such as those over the evaluation of triggering events requiring impairment testing for goodwill or long-lived assets. The relevant internal controls over these estimates often involve management review controls. It will be important for entities to consider if the design and operation of such internal controls require enhancement to enable appropriate, and documented, consideration of issues arising from the pandemic.

For additional COVID-19–related ICFR considerations, please refer to Deloitte's *Reacting to COVID-19 in internal control over financial reporting*.

FERC reporting considerations

FERC form filing due date extension

On March 19, 2020, the FERC issued a notice that there will be an extension of time to provide more flexibility on deadlines for certain required filings, including Form 1, Form 2, and Form 60. Form 1 and Form 2 are now due on or before May 1, 2020. Form 60 was subject to a second extension on April 2, 2020, and is now due on or before June 1, 2020. Form 6 was specifically excluded from the notice and continues to be due on April 20, 2020. The filings extended to May 1 include nonstatutory items required by the Commission, such as compliance filings, responses to deficiency letters, and rulemaking comments, as well as certain forms required by the Commission. The deadline extension also will apply to filings required by entities' tariffs or rate schedules. Beyond the extensions provided by the March 19 and April 2 notices, entities may seek extensions for other deadlines and may seek waiver of Commission orders, regulations, tariffs, and rate schedules.

Additionally, the FERC issued several orders and policy statements on April 2, 2020, offering relief to companies. In its policy statement (FERC docket PL20-5-000), the FERC indicated it will give highest priority to processing filings related to the reliable operation of energy infrastructure during the pandemic and will "expeditiously review and act on requests for relief, including, but not limited to, requests for cost recovery necessary to assure business continuity of the regulated entities' energy infrastructure in response to the national emergency."

The FERC also issued an order granting a blanket waiver of the requirement to hold in-person meetings and provide notarized documents in open access transmission tariffs (FERC docket EL20-37-000). The waiver is in place through September 1, 2020. The commission did note, however, that grid operators must still hold meetings consistent with their tariffs by other means, such as over the phone or virtually.

In another order (FERC docket RM 17-2-000), the FERC extended the time period for RTOs and ISOs to publicly post uplift reports and operator-initiated commitment reports. The initial timeline required these reports to be posted between April 2020 and September 2020, and the order extends the window to October 20, 2020. This order does not prohibit RTOs and ISOs from posting these reports before October 20, 2020, or prohibit them from seeking further extension of time if needed.

Finally, in an effort to prioritize requests during the pandemic, the FERC has delegated authority to the director of FERC's Office of Energy Market Regulation to act on uncontested requests for prospective waiver of certain regulatory obligations (FERC docket AD20-13-000) and to the director of FERC's Office of Energy Policy and Innovation to act on motions for extension of time to file, or requests or petitions for waiver of the requirement of, FERC Form No. 552 Annual Report of Natural Gas Transactions and FERC-730 Report of Transmission Investment Activity (FERC docket RM20-13-000).

AFUDC

Individuals at public utilities responsible for the calculation of AFUDC should consider FERC guidance on the subject. Utilities may have ceased construction due to COVID-related work stoppages. The 2011 FERC Accounting Release, AI11-1-000, states, "The capitalization period for AFUDC shall begin when two conditions are present: (1) capital expenditures for the project have been incurred; and (2) activities that are necessary to get the construction project ready for its intended use are in progress. AFUDC capitalization shall continue as long as these two conditions are present." It also states, "No AFUDC should be accrued during periods of interrupted construction unless the company can justify the interruption as being reasonable under the circumstances."

Accounting personnel should determine if AFUDC should continue to be accrued during the period asset construction is paused. Past regulatory precedent and the utility's assertions around probability of recovery of AFUDC should factor in the determination.

Acknowledgments

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