



Understanding and Applying FERC Accounting Standards

Presenters

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Background

Applications

Standards

Further Guidance

Alphabet Soup



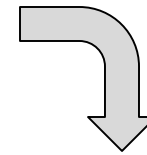
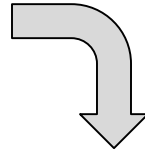
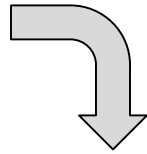
Basis of FERC Accounting Standards

- Congress regulates interstate commerce
 - Interstate Commerce Act (1887) (ICA, established ICC)
 - Dept. of Energy Organization Act (1977) (established FERC)
 - Energy Policy Act of 1992 (led to Orders 561, 571-72)
- FERC administers oil pipeline regulation
 - Reporting – 18 CFR 357
 - Accounting – 18 CFR 352
 - Record retention – 18 CFR 356
 - Depreciation studies – 18 CFR 347

Cite this Code: CFR

To cite the regulations in this volume use title, part and section number. Thus, 18 CFR 1.101 refers to title 18, part 1, section 101.

Basis of FERC Accounting Standards



CODE OF FEDERAL REGULATIONS

FERC Oil Pipeline Regulations

- 18 CFR 340-41, 344

Tariff filing and administration

- 18 CFR 342, 346, 348

Rate setting methodologies (indexing, market-based rates, settlement, cost of service)

- 18 CFR 349

Audit procedures – notice, findings, response

- **18 CFR 352 – The Uniform System of Accounts (USoA)**

- **18 CFR 347, 351, 356-357**

Other accounting regulations

The Uniform System of Accounts

- 18 CFR 352 – the “USoA” or “USofA”

- Structure

- Definitions

Affiliated companies, Book cost, Carrier, Control, Cost, Date of retirement, Depreciation, Group plan, Investor, Replacement, Service life

- General Instructions

Classification | Records | Period | Extraordinary items
Property acquired | Transactions with affiliates
Depreciation | Operating revenues and expenses

- Account descriptions

The required chart of accounts

The Uniform System of Accounts

- Pervasive considerations
 - Classification per USoA
 - Carrier / Noncarrier
 - Crude / Products
 - Trunk / Gathering / Delivery / General
 - Operations & Maintenance / General
 - Records maintained, not just reporting standards
 - Period, on a monthly basis within 60 days
 - Just and Reasonable Charges
 - “...not to exceed amounts necessary to the honest and efficient operations of carrier business”
 - “...payments in excess of such just and reasonable charges shall be included in account 660, Miscellaneous Income Charges

Annual and Quarterly Reports

FERC Form No. 6 (“Form 6” and “Form 6-Q”)

- 18 CFR 357
- Annual Form 6 – due April 18
- Qs due 70 days after quarter end
 - Q1 due June 9th
 - Q2 due September 8th
 - Q3 due December 9th

Record Retention Rules

■ 18 CFR 356

- | | |
|------------------------------|--|
| ■ Board minutes | 5 years |
| ■ Long term debt records | 6 years after redemption |
| ■ Ledgers and journals | 3 years |
| ■ Vouchers | 5 years |
| ■ Property records | 3 years after disposition |
| ■ Payroll records | 3 years |
| ■ Oil transportation records | 3 years |
| ■ Tariff copies | 3 years after cancellation
or termination |

AOPL - Oil Pipeline Industry Accounting Guideline (OPIAG)

- Industry-sponsored interpretation of regulatory accounting standards
- Established and developed by the AOPL Accounting Committee
- Singular interpretation and standard implementation approach for accounting regulations identified as lacking in clarity
- Not intended to run counter to Commission standards set forth in orders or regulations
- Used by Commission staff in the audit process and have been referenced in audit reports

Other Training Courses

- AOPL conducts a full-day Form 6 training course (typically held in February)
 - How to develop data needed for Form 6 reporting
 - Covers all aspects of the Form 6
- Today's session is more conceptual (and shorter) than the Form 6 training course
- FERC Audits and Compliance Conference (February/March)
- Related courses at this Annual Business Conference



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Settings that Require FERC Accounting Standards

- Form 6 annual and quarterly reports
- FERC compliance plan (and audit responses)
- Cost of service development
- Depreciation studies
- Requests for approval of accounting
- Cash management program disclosures

Annual and Quarterly Reports



**FERC Financial Report
FERC Form No. 6: ANNUAL REPORT
OF OIL PIPELINE COMPANIES and
Supplemental Form 6-Q:
Quarterly Financial Report**

(Formerly ICC Form P)

Purpose of the Form 6

- “Designed to collect financial and operational information” (Form 6, page *i*, Purpose)
 - Report the carrier’s financial position and operating performance
 - Enable FERC to evaluate the rate index
 - Enable interested parties to determine whether to challenge indexed- or cost-based rates
 - Compare financial performance and results of operations among regulated entities

Primary Users of Form 6 Data

1

FERC

2

Shippers

3

Other Carriers and AOPL

4

**Other Regulatory Commissions
and Taxing Authorities**

Filing Requirements

Revenue ¹	Requirement
Greater than \$500k	Complete Form 6
Between \$350k and \$500k	Page 301 (Revenues) Page 700 (Cost of Service)
Less than \$350k	Page 700 (Cost of Service)

¹ FERC jurisdictional operating revenue for each of the three previous calendar years.

Information Reported in Form 6

Category	Key Schedules	# of Form 6 Schedules	# of Form 6-Q Schedules
General Corporate Info and Financial Statements	<ul style="list-style-type: none"> • Ownership info, addresses, etc. • Balance Sheet, Income Stmt, etc. • Notes, important changes, etc. 	14	7
Balance Sheet Supporting Schedules	<ul style="list-style-type: none"> • Carrier property and accrued depreciation data • Undivided joint interest (UJI) data • Affiliated payables/receivables 	19	0
Income Account Supporting Schedules	<ul style="list-style-type: none"> • Revenues • Operating expenses 	7	2
Plant Statistical Data	<ul style="list-style-type: none"> • Cost of Service (Page 700) • Statistics of Operations • Miles of Pipeline Operated • Footnotes 	4	1
	Total Schedules	44	10

Form 6 Submission Data Validation

- Developed to assist with Form 6 accuracy and internal consistency – performs ~80 separate validations
- Includes both annual and quarterly validations
- Designed for efficient data input
- Enhanced validation numbering via formulas and conditional formatting

Form 6 Submission Data Validation

- Excel-based tool available to AOPL members
- Request workbook via email from:

Sacha Kathuria

skathuria@aopl.org

Thank you, Sacha!

FERC Compliance Audits

- Four Completed – Enterprise, Colonial (2014-15); Enbridge, Plantation (~2015-16)
- Three in process – Plains, Marathon, Explorer (~2016-17)
- Comprehensive in scope – evaluate compliance with all Commission regulations for oil pipeline companies: 18 CFR 340-357
- Includes broad review and evaluation of regulatory practices and compliance processes

FERC Compliance Audits

Include compliance with the following areas:

- **Accounting and Financial Reporting**
 - Ensure compliance with USofA
 - Review Form No. 6 and Page 700
 - Review allocations, shared services, etc.
- **FERC Regulatory Compliance Program**
 - Ensure consistency with FERC Policy Statement on Enforcement of Statutes
 - Adequacy of procedures and controls
 - Internal Audit Department reports
- **Pipeline Operations**
 - Review nominations, scheduling and billing
 - Capacity Allocation and Lottery Process
- **Training**
 - Ensure proper training of regulations, processes, and procedures

Supporting Documentation

“Each carrier shall keep its books of account, and all other books, records and memoranda which support the entries in such books of account, so as to be able to **furnish readily full information** as to any item included in any account. Each entry shall be supported by such detailed information as will permit ready identification, analysis, and verification of all facts relevant thereto.”

18 CFR 352 1-2(a)

Cost of Service Development

- Operating expenses flow directly
- Property records support rate base development
 - Discrete capitalized interest
 - Purchase accounting adjustments
- Consistency year-over-year permits normalization
- Shared cost allocations can involve parent company accounts
- Charges are subject to the “just and reasonable” provision (18 CFR 352.1-14)

Depreciation Studies

- Instruction 1–8(b), Depreciation Accounting–Rates
 - “Carriers becoming subject to this system of accounts ... shall file, within six months, composite annual depreciation rates applicable to the book cost of each class of depreciable carrier property as will distribute the service value, by the straight-line method, in equal annual charges ... during the service life of the property.”
 - “Carriers shall base ... rates on estimated service values and service lives developed from engineering and other studies.”
- 18 CFR 347 sets forth support required in a depreciation study

Requests for Approval of Accounting

Formal requests to the FERC Chief Accountant:

- Seek approval of journal entries to record a business combination
- Request permission to use certain accounts
- Exception to record gain or loss on disposition of property
- Other specific guidance

Requests for Approval of Accounting

Required for use of accounts

- Unusual or infrequent items (645 or 665)
- Extraordinary items (680)
- Income (loss) from discontinued segments (675)
- Cumulative effect of changes in accounting principles (697)
- Prior period adjustments to retained earnings (705)
- Other credits/debits to retained income (710/720)
- Transfers between APIC and Unappropriated RE (73 and 75)

Cash Management Disclosure

- Oil pipeline companies that participate in cash management programs must disclose those programs to the FERC. (18 CFR 357.5)
- Due within 10 days of effective date—initial and subsequent changes
- If proprietary capital ratio drops below 30%, must note in Form 6
 - Generally, the ratio of total proprietary capital to the sum of total proprietary capital and total long-term debt



Background

Applications



Standards

Further Guidance

FERC Accounting Standards

- **Objectives and Principles**
- Acquisitions and Investments
- Property
 - Capitalization
 - Depreciation
 - Disposition
- Revenues and Expenses

Objectives and Principles

GAAP	USoA
<ul style="list-style-type: none">• Present information that is useful to lenders and investors (present and potential)• Financial position, performance<ul style="list-style-type: none">• Assets, liabilities, equity• Revenues, expenses, gains, and losses (and other)• Conceptual framework<ul style="list-style-type: none">• Fundamental characteristics<ul style="list-style-type: none">• Relevance• Faithful Representation• Enhancing characteristics<ul style="list-style-type: none">• Comparability• Timeliness• Understandability• Pervasive constraints (materiality, benefits/costs, practice)	<ul style="list-style-type: none">• Present financial and operating information that is useful to FERC• All financial information necessary to assist the FERC in its regulation of oil pipelines<ul style="list-style-type: none">• Financial statements• Supporting schedules• Statistical pages• Cost of service analysis• Major sections<ul style="list-style-type: none">• Defined terms• General instructions• Account descriptions

Objectives and Principles

GAAP	USoA
<ul style="list-style-type: none">• Accounting Standards Codification (ASC)• Interpretation of management and external auditors• U.S Securities and Exchange Commission (“SEC”)<ul style="list-style-type: none">• SEC Final Rules• Division of Corporation Finance – Financial Reporting Manual	<ul style="list-style-type: none">• 18 CFR 352 (USoA)• Additional guidance in accounting pronouncements and interpretations issued by FERC• Interpretation of Chief Accountant• AOPL - Oil Pipeline Industry Accounting Guideline

Objectives and Principles

General Reporting Guidelines

GAAP	USoA
<ul style="list-style-type: none">• Report in audited financial statements• Extensive disclosure requirements• Chart of accounts developed by company• Report by consolidated legal entity and business segment	<ul style="list-style-type: none">• Report on Form 6• Required supporting schedules• Chart of Accounts prescribed by FERC in the USoA• Report by tariff-filing legal entity, report carrier/noncarrier and inter-/intra-state

Objectives and Principles

Materiality

GAAP	USoA
<ul style="list-style-type: none">• A material difference is one large enough to affect decisions of financial statement users• Materiality of items is evaluated both individually and in the aggregate• Evaluate from both a qualitative and quantitative perspective• Auditor's cite materiality in the opinions they offer	<ul style="list-style-type: none">• 10 percent of net income: <i>As a general standard an item [is] material when it exceeds 10 percent of annual income (loss) before extraordinary items. 18 CFR 352.1-6(f)</i>• Considered individually and not in the aggregate, unless arising from a single event or plan of action.• Signing company officer certifies that Form 6 conforms with USoA "in all material respects"

FERC Accounting Standards

- Objectives and Principles
- **Acquisitions and Investments**
- Property
 - Capitalization
 - Depreciation
 - Disposition
- Revenues and Expenses

Business Combinations

GAAP	USoA
<ul style="list-style-type: none"> • Reporting entity—generally parent • Assets generally¹ recognized at fair value on the acquisition date (purchase/acquisition method) • Original cost carries no significance, is not maintained in records • Goodwill recorded, but not amortized 	<ul style="list-style-type: none"> • Reporting entity—generally sub; therefore, question of pushdown accounting arises (USoA is silent) • Purchase method² (lingering provision for pooling possible interests) • Original cost must be retained for cost of service, but generally not used in reporting • Goodwill recorded, amortized to account 660, Misc Income Charges

¹ Certain transactions associated with business combinations do not meet the requirements to be accounted for as business combinations under the acquisition method (see ASC 805-10-05-1).

² **Tentative journal entries should be submitted to FERC.**

Equity Investments

GAAP	USoA
<ul style="list-style-type: none">• Based upon ownership and control, equity interests may be accounted for as a controlled subsidiary, an equity method investment, or an available-for-sale security (FMV).• Must determine whether equity interests represent a controlling financial interest that requires consolidation of the entity under ASC 810.	<ul style="list-style-type: none">• Regardless of ownership and control, carriers use the equity method of accounting for: all investments in corporate joint ventures and all investments in voting stock of affiliated companies giving the carrier the ability to significantly influence the operating and financial policies of an investee. (see 18 CFR 352 2-2(c) and Colonial Audit Report).• A carrier can attempt to request a waiver of these requirements from the Commission.• Undivided joint interest property reported separately.

Equity Accounting Under USoA

- Prescribed investment accounts are insufficient
- Equity accounting under USoA requires a reporting worksheet or memorandum accounts
 - An investment account
 - An income account
 - A retained income account
 - Possibly other memorandum accounts

(see 18 CFR §352 2-2(c) and Colonial Audit Report)

FERC Accounting Standards

- Objectives and Principles
- Acquisitions and Investments
- **Property**
 - Capitalization
 - Depreciation
 - Disposition
- Revenues and Expenses

Property Accounting Classification

GAAP	USoA
<ul style="list-style-type: none">• Not specified. Reporting generally follows classes defined by function and common useful life.	<ul style="list-style-type: none">• Specific carrier accounts prescribed• Categorized by:<ul style="list-style-type: none">– Carrier / Noncarrier– Asset class (group)– Gathering / Trunk / General

Property Accounting

Property Acquired

GAAP	USoA
<ul style="list-style-type: none">• In a business combination, assets generally recorded at their acquisition-date fair values (ASC 805-20-30-1)• Outside of a business combination, assets recorded at purchase price	<ul style="list-style-type: none">• Assets generally recorded at acquisition price• Purchase price apportioned to individual FERC accounts¹ based on ratio of purchase price and (1) original cost or (2) fair value of properties• Property acquired from an affiliate recorded as it was recorded on the books of the affiliate (transfer)

¹ Unless costs of transportation property, by group, are specified in acquisition agreement.

Property Accounting

Property Constructed

GAAP	USoA
<ul style="list-style-type: none">• General rule is that all costs associated with preparing an asset for its intended use are costs of that asset• Some carriers assign a portion of overhead to the constructed asset	<ul style="list-style-type: none">• Includes following costs:<ul style="list-style-type: none">– Cost of labor (not incidental)– Cost of materials and supplies– Cost of special machine service– Cost of transportation– Cost of contract work– Cost of protection– Cost of injuries and damages– Cost of privileges and permits– Taxes– Rent– Interest during construction– Cost of disposing of excavated material– Asset retirement costs– Overhead per Opinion 511A

Property Accounting

Threshold for Capitalization

GAAP	USoA
<ul style="list-style-type: none">• Capitalization policy designed to follow FASB concepts, including materiality• Expenditure meets definition of asset and recognition criteria<ul style="list-style-type: none">• Probable future benefit• Rights to that benefit arise from past transaction• Benefits can be measured reliably	<ul style="list-style-type: none">• Must maintain a written units of property listing for use in accounting for additions and retirements of carrier plant and apply the listing consistently• No materiality criteria set by FERC• No conflict with GAAP

Property Accounting

Capital vs. Expense (USoA Approach)

- ***Replacements*** – capitalize if the expenditure is for the substantial replacement of a unit of property, or it will materially improve, enhance, or better the asset
- ***Inspection and repairs*** – the cost of reopening trenches for repairs, or installation of casing, coating or cathodic protection, and the necessary backfilling shall be charged to maintenance expense

Property Accounting

Capital vs. Expense (USoA Approach)

■ *Pipeline Assessment Cost*

- Cost of periodic inspections expensed
 - Based on DOT's testing guidelines, costs represent regularly recurring costs
 - May lead to activity that is capitalized (e.g., replacement of pipe)
- See Order on Accounting for Assessment Costs (Dkt. AI05-1-000, June 30, 2005)

Property Accounting

Depreciation Rates

GAAP	USoA
<ul style="list-style-type: none">• Rates typically calculated by using component rates based on useful life of specific asset• Component rate applied to net book value• Companies revise depreciation rates if appropriate• Cease depreciation when asset is fully depreciated	<ul style="list-style-type: none">• Composite straight-line rates on “group plan of accounting”; generally each FERC account is a group• Composite rate applied to gross book value• Rates require approval of FERC depreciation study• Cease depreciation when group is fully depreciated

Property Accounting

Acquisition Example—Prompt

■ Stylized Fact Pattern

- Initial construction at a cost of \$60.0 million
- Sold at the end of year 10 for \$90.0 million
- FERC approved 3.33% depreciation rate (buyer and seller)
- Financial accounting depreciation based on 20-year overall service life (buyer and seller)

■ Assignment

- In three columns (GAAP, FERC book, and FERC cost-of-service) show plant and accumulated depreciation balances for the seller just prior to sale (end of 10) and the buyer one year later (end of 11).

Property Accounting

Acquisition Example—Solution

Seller balances – end of year 10

	GAAP	FERC (p212)	COS (p700)
Plant	\$ 60.0	\$ 60.0	\$ 60.0
A/D	\$ 30.0	\$ 20.0	\$ 20.0
Net book	\$ 30.0	\$ 40.0	\$ 40.0

Buyer balances – end of year 11

	GAAP	FERC (p212)	COS (p700)
Plant	\$ 90.0	\$ 90.0	\$ 60.0
A/D	\$ 9.0	\$ 3.0	\$ 22.0
Net book	\$ 81.0	\$ 87.0	\$ 38.0

Property Accounting

Sales and Retirements

GAAP	USoA
<ul style="list-style-type: none">Gain/loss on sale/retirement of depreciable property typically recorded in income	<ul style="list-style-type: none">Gain/loss on sale/retirement of depreciable property charged to accrued depreciation¹ per the group plan of accounting

¹ Need FERC approval for exception to rule (e.g., discontinued segment, extraordinary item, etc.).

Property Accounting

Retirement Example—Prompt

■ Stylized Fact Pattern

- Initial constructed at a cost of \$60.0 million
- At the end of year 10, retired \$12.0 million
- FERC approved 3.33% depreciation rate
- Financial accounting depreciation based on 20-year overall service life

■ Assignment

- In four columns show plant and accumulated depreciation balances for before and after the retirement on GAAP and FERC books.

Property Accounting

Retirement Example—Solution

GAAP balances

	Before	After
Plant	\$ 60.0	\$ 48.0
A/D	\$ 30.0	\$ 24.0
Net book	\$ 30.0	\$ 24.0

- Still 50% depreciated
- Loss of \$6 million on disposal

FERC balances

	Before	After
Plant	\$ 60.0	\$ 48.0
A/D	\$ 20.0	\$ 8.0
Net book	\$ 40.0	\$ 40.0

- Still net book of \$40.0 million
- Both balances reduced by \$12.0 million

Property Accounting

Transfers to Noncarrier Property

GAAP	USoA
<ul style="list-style-type: none">• NA	<ul style="list-style-type: none">• Transfer past accrued depreciation to noncarrier property (unlike retirements under group method of depreciation)• Transfer gross book cost to noncarrier property

Property Accounting

Cost of Removal / Net Salvage

- “Cost of removal means cost of demolishing, dismantling, tearing down, or otherwise removing property including costs of handling and transportation. It does not include the cost of removal activities associated with asset retirement obligations.” (18 CFR 352 Definitions 12)
- “Net salvage value means salvage value of property retired less the cost of removal.” (18 CFR 352 Definitions 20)

Property Accounting

Cost of Removal / Net Salvage

- Per Enterprise Audit Report (FA-14-1-000)
 - “Under the Commission’s accounting requirements, cost of removal and net salvage are two components of net salvage ... Actual net salvage, positive or negative, is credited or debited, respectively, to the accumulated reserve for depreciation when incurred.”

Insurance Proceeds

“In case of casualty loss, insurance proceeds recovered shall be credited to account 31, Accrued Depreciation—Carrier Property, in an amount not to exceed the book cost of the property involved. Any excess amount shall be credited to account 640, Miscellaneous Income.”

18 CFR 352 3-7(b)(2)

FERC Accounting Standards

- Objectives and Principles
- Acquisitions and Investments
- Property
 - Capitalization
 - Depreciation
 - Disposition
- **Revenues and Expenses**

Revenue Accounting Classification

GAAP	USoA
<ul style="list-style-type: none">• No standard, detail generally limited	<ul style="list-style-type: none">• Specific revenue accounts are prescribed by the FERC<ul style="list-style-type: none">– Carrier / Noncarrier– Gathering / Trunk / Delivery / Allowance / Storage / Rental / Incidental• Further categories required for Form 6 reporting<ul style="list-style-type: none">– Crude / Products– Interstate / Intrastate - (Gathering, Trunk, Delivery only)

Operating Expenses Classification

GAAP	USoA
<ul style="list-style-type: none">• No standard, detail generally limited	<ul style="list-style-type: none">• Specific operating expense accounts are prescribed by the FERC• Categorized by:<ul style="list-style-type: none">– FERC account – O&M and General accounts– Gathering lines, trunk lines, and delivery– Crude oil lines and product lines

Operating Expenses

OpEx vs Miscellaneous Income Charges

GAAP	USoA
<ul style="list-style-type: none">• Companies include certain costs within OpEx	<ul style="list-style-type: none">• Recent audit findings suggest the need for discretion regarding costs associated with political donations, charitable contributions, and lobbying expenses (and potentially other costs)• They may require exclusion from OpEx and instead be included in Miscellaneous Income Charges• Impacts cost of service on page 700

Operating Expenses

Affiliate transactions

GAAP	USoA
<ul style="list-style-type: none">• Some companies account for transactions at cost plus incidental fee, others use fair-market value, and there are other practices as well	<ul style="list-style-type: none">• Any differences between actual transaction price and the lower of actual costs or estimated fair market value are considered to be of a financing nature and are recorded as non-operating charges or credits• Carrier must maintain records and supporting data in a separate file



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Further Guidance

Carrier vs. Noncarrier Property

- Define carrier property
 - Carrier FERC-defined as “subject to Interstate Commerce Act”
 - Would exclude intrastate-only and nonregulated assets
- Resolution
 - Property held for purpose of providing common carrier pipeline service is Carrier Property.

Operating vs. Noncarrier Revenue

- Distinguish operating from noncarrier revenue
- Resolution
 - Rule: Asset type → Revenue type
 - Carrier property → Operating Revenue
 - Noncarrier property → Noncarrier Revenue
 - Exception:
 - Disassociation w/carrier operations → Noncarrier

Operating and Maintenance vs. General Expenses

- Distinguish Operating and Maintenance (300s) expenses from General (500s)
- Resolution – should be based on
 - Function
 - Physical location (example, field/central)
 - Related-property classification



Specific Classification Items

- Fines and Penalties
- Drag reducing agent
- Materials and supplies
- Casualty and other losses
- FERC annual charges
- Equity reporting for non-corporate filers