FW: Financing of a regulatory asset

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From: Picard, Michel
Sent: Monday, February 13, 2017 1:00 PM
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Subject: Financing of a regulatory asset

Alec, John,

The issue is the following:

- IESO, the System operator, has been asked by the province of Ontario to delay the recovery of 10% of the energy purchased from the generators.
- The 10% will be financed by Ontario Power Generation (OPG) and will be recovered over a period of 20-30 years to smooth the impact on rates.
- IESO and OPG are both rate-regulated by the Ontario Energy Board (OEB).
- IESO is an agent to the market participants – ie. IESO records the energy transactions on a net basis – since it is a pass-through there is no net impact on the statement of income.
- IESO currently recovers most of the energy costs paid to the generators in the same month with the remaining amount being recovered in the following month.

The journal entries to reflect the above discussion are as follows:

1. to record the energy purchased from generators

   Dr Energy purchased 100
   Cr Generators 100

2. to record the amount collected from the distributors

   Dr Cash 90
   Cr Revenue 90

3. to record the remaining amount to be collected from the distributors over a period of 20-30 years in accordance with legislation and the OEB 's direction

   Dr Regulatory asset 10 Can IESO record a regulatory asset?
   Cr Revenue 10

4. to record the cash received from OPG to finance the remaining 10% payments to the generators

   Dr Cash rec'd OPG 10
   Cr Due to OPG 10 The alternative is to eliminate the regulatory asset instead of creating a liability.

5. to record the payments to generators

   Dr Generators 100
   Cr Cash 100

As noted in the example above, there are a few questions that I need to address.

1. Although IESO is rate-regulated, can it recognize a regulatory asset for the pass-through? The issue at play is that IESO is an agent of the market participants and the definition of a regulatory asset under ASC 980 requires to be an incurred cost by IESO.
2. Assuming IESO can recognize a regulatory asset for the 10% of the uncollected energy costs, does IESO derecognize the regulatory asset when IESO receives the cash from OPG? Or does it maintains the regulatory asset and records cash with an offsetting liability to OPG?
3. What type of asset will OPG recognize? A regulatory asset or an intangible asset?

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