

Allowance for Funds Used During Construction (AFUDC)

SUMMARY

This standard establishes an enterprise-wide framework in the area of accounting for property, plant and equipment (PP&E), issued by PG&E Corporation and its affiliates and subsidiaries, including Pacific Gas and Electric Company. This standard provides the requirements and responsibilities related to the Allowance for Funds Used During Construction (AFUDC).

It is important that these requirements and responsibilities be adhered to, in order to diminish the risks related to inappropriate accounting for AFUDC. The following are risks related to AFUDC.

1. Financial Risk

AFUDC must be recorded correctly to avoid misstatements of plant and Construction Work in Progress (CWIP) balances, as well as misstatements of AFUDC income.

2. Regulatory Risk

AFUDC must be recorded correctly in order to avoid the over-collection or under-collection of such costs from ratepayers.

TARGET AUDIENCE

All utility employees that are responsible for planning or managing capital projects. These employees are referred to as “job owners” in this standard. This standard also applies to employees responsible for computing and monitoring AFUDC rates.

SAFETY

N/A

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REQUIREMENTS

1 Accounting for AFUDC

- 1.1 Costs incurred for capital projects with construction periods of 30 days or greater must be accounted for as follows:
1. Recorded in CWIP
 2. Accrue AFUDC over the life of the project, from the date when the first cost is posted to the order until the date when the installed assets become used and useful in providing utility service (i.e., operative date).
 - a. Refer to [Appendix 1 – Construction Period for Determination of Order Type](#).
 - b. Refer to FERC Plant Instruction 3 (17) for guidance on computing AFUDC.

2 Computing AFUDC Rates

- 2.1 Asset Accounting is responsible for AFUDC rates as follows:
1. Computing and posting monthly actual AFUDC rates into SAP in accordance with FERC Plant Instruction 3 (17) AND [FIN- 3706P-01 AFUDC Calculation Procedure](#).
 2. Any deviation, exception or modification to the AFUDC rate calculation must require preapproval from the FERC Chief Accountant.
 3. Updating the [Attachment 1 – AFUDC Application Factor](#) with the annual planned AFUDC rates that reflect PG&E's weighted average cost of capital as approved by the California Public Utilities Commission (CPUC) in the Cost of Capital Proceeding.
- 2.2 Per Order No. 561, AFUDC should be compounded semiannually
1. Order No.561 states: “[W]e believe that a monthly compounding of AFUDC... may result in excessive amounts of capitalized since cash outlays for interest and dividends are not normally made on a monthly basis. We shall therefore permit compounding but no more frequently than semiannually”
Amendments to Uniform System of Accounts for Public Utilities and Licensee and Natural Gas Companies, Order No.561, 57 FPC 608, 612 (1977), *reh'g denied*, Order No. 561-A, 59 FPC 1340 (1977)
 2. See attachments for additional references on Order No. 561 guidance:

[Attachment 2: FERC Doc No. ER05-17-007](#) – see page 2

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[Attachment 3: Kuparuk Transportation Company Initial Decision](#) – see page 18

3 Assigning Order Types

- 3.1 Job Owners are responsible for assigning Order Types to capital orders as follows:
1. Ensuring that capital projects with planned construction periods of 30 days or greater are recorded in capital orders that accrue AFUDC.
 - a. These orders are identified in the accounting system with Order Types of "70", OR with 30 Day Indicators of "Y".
 - Refer to [Appendix 1 – Construction Period for Determination of Order Type](#).
 2. Ensuring that costs of capital projects with planned construction periods of less than 30 days are recorded in capital orders that do NOT accrue AFUDC.
 - a. These orders are identified in the accounting system with Order Types of "10" or "60", OR with 30 Day Indicators of "N".
 - b. Refer to [Appendix 1 – Construction Period for Determination of Order Type](#).

4 Assigning Operative Dates

- 4.1 For capital projects with planned construction periods of 30 days or greater, Job Owners are responsible for assigning operative dates to capital orders as follows:
1. Entering into capital orders the operative dates which reflect the dates when the installed assets became used AND useful in providing utility service.
 - a. Operative dates are required to stop AFUDC from accruing in the accounting system.
 - b. Refer to [Capital Accounting Instructions, FAQ - Operative Date](#) for additional guidance on assigning accurate operative dates.

5 AFUDC Monitoring and Error Correction Responsibilities

- 5.1 Job Owners are responsible for AFUDC monitoring and correction of errors as follows:
1. Verifying that AFUDC has accrued on capital orders with planned construction periods of 30 days or greater.
 2. Verifying that AFUDC has stopped accruing on capital orders when the installed assets became used and useful (i.e., operative dates were assigned).

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3. Verifying that AFUDC has not accruing on capital orders with planned construction periods of less than 30 days.
 4. Notifying Capital Accounting of any potential errors due to incorrect order types or operative dates.
 5. Identifying capital projects with extended periods of interrupted construction.
 - a. Refer to [FIN-3807S Capital Order Management Standard](#) Section 4 for guidance in determining if AFUDC should be suspended by placing an order into deferred status.
- 5.2 Capital Recovery is responsible for AFUDC monitoring as follows:
1. Monitoring budget vs. actual AFUDC costs variances.
 2. Notifying Asset Accounting of any potential errors due to incorrect order types or operative dates.
- 5.3 Asset Accounting is responsible for correcting significant AFUDC errors when errors are detected.

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END of Requirements

DEFINITIONS

Allowance for Funds used During Construction (AFUDC): Capitalized financing costs that are recorded in CWIP during the period when new plant assets are being constructed. AFUDC ceases when the assets become operational and transfer from CWIP to plant. AFUDC is recovered in customer rates through depreciation expense. The monthly rates that are used to compute AFUDC reflect PG&E's weighted average cost of capital for both debt and equity. The FERC approves the formula for computing AFUDC, while the CPUC approves the cost of equity rate.

Allowance for Funds used During Construction (AFUDC) Planning Rate: Rate used to forecast AFUDC for project approvals, annual budgeting, and other planning purposes. The rate is computed annually to reflect PG&E's weighted average cost of capital as approved by the California Public Utilities Commission (CPUC) in the Cost of Capital Proceeding. The current rate is included in the [Attachment 1 – AFUDC Application Factor](#) spreadsheet.

Capital Order: An order that tracks all costs (net of billing credits) that are incurred to install and/or remove capital retirement units, which are listed in PG&E's Retirement Units Catalog (RUC). The order settlement rules/unit estimates direct the installation costs to plant accounts and direct the removal costs to accumulated depreciation.

Construction Period: Number of days which starts when physical construction begins on a capital order and ends when the constructed assets are placed into service (i.e. operative date). As described in [Appendix 1 – Construction Period for Determination of Order Type](#), order types are assigned to capital orders during the project planning phase based upon the expected duration of the planned construction period:

- Order Types of "70", or with 30 Day Indicators of "Y" are assigned to orders with planned construction periods of 30 days or greater (these orders accrue AFUDC).
- Order Types of "10" or "60", or with 30 Day Indicators of "N" are assigned to orders with planned construction periods of less than 30 days (these orders do not accrue AFUDC).

Construction Work In Progress (CWIP): An account that is used to record the balance of capital work orders which track the costs of plant in the process of construction. Work order balances are transferred from CWIP to Plant in Service when construction is completed and the installed assets became used and useful in providing utility service (i.e., at the operative date)

Operative Date: The date when a newly constructed or acquired asset becomes used and useful in providing utility service. The operative date stops AFUDC from accruing in the accounting system and triggers the transfer of the order costs from CWIP to Plant in Service.

Plant in Service: An account that is used to record the costs of plant assets currently in service. These assets are recorded at their original acquisition or installation cost.

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IMPLEMENTATION RESPONSIBILITIES

Capital Accounting Advice is responsible for issuing the standard and providing communication, guidance, and training to job owners.

Asset Accounting is responsible for computing actual and planned AFUDC rates in accordance with this standard.

Job owners are responsible for accurately managing capital projects so that AFUDC is accurately recorded in accordance with this standard.

GOVERNING DOCUMENT

N/A

COMPLIANCE REQUIREMENT / REGULATORY COMMITMENT

- FERC Uniform System of Accounts, 18 CFR, Chapter I, Part 101 Electric Plant Instructions 3 (17), Components of Construction Costs - Allowance for Funds Used During Construction
- FERC Accounting Release No. 5, Capitalization of Allowance for Funds Used During Construction
- Securities Act of 1933
- Securities Exchange Act of 1934

REFERENCE DOCUMENTSDEVELOPMENTAL REFERENCES:

Developmental References:

N/A

Supplemental References:

[FIN- 3706P-01 AFUDC Calculation Procedure](#)

[FIN-3807S Capital Order Management Standard](#)

[Capital Accounting Instructions, FAQ - Operative Date](#)

APPENDICES

[Appendix 1 Construction Period for Determination of Order Type](#)

Allowance for Funds Used During Construction (AFUDC)**ATTACHMENTS**[Attachment 1 - AFUDC Application Factor](#)[Attachment 2 – FERC Doc No. ER05-17-007](#)[Attachment 3 – Kuparuk Transportation Company Initial Decision](#)**DOCUMENT REVISION**

N/A

DOCUMENT APPROVER

[REDACTED], Director, Capital Accounting

DOCUMENT OWNER

[REDACTED], Manager, Capital Accounting Advice

DOCUMENT CONTACT

[REDACTED], Manager, Capital Accounting Advice

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REVISION NOTES

Where?	What Changed?
Section 5.5.a	Replaced reference link from “FIN-3807P-01 Deferred Order Procedure” to “FIN-3807S Capital Order Management Standard”
Supplemental References	Replaced reference link from “FIN-3807P-01 Deferred Order Procedure” to “FIN-3807S Capital Order Management Standard”
Attachment 1	Updated “Rate” and “Project Period” in AFUDC Application Factor
Documented Owner	Updated
Documented Contacts	Updated

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Appendix 1, CONSTRUCTION PERIOD FOR DETERMINATION OF ORDER TYPE

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The Order Period determines how long the capital order, with a construction period greater than 30 days, will accrue AFUDC. The order period starts the first month when costs are charged to the order and continues until the month the order is declared operational. AFUDC should be accrued from the month costs are first charged to the order, even if the actual construction starts later.

Estimated Construction Period determines capital order type. Construction Period starts when the physical construction begins and ends when the asset is placed into service (i.e. operative date). The continuous Construction Period should be used to determine the order type to be set up for capital orders (i.e. type 60, 70 or PM orders with "Y" or "N" for 30-day indicator).

Usually the Order Period is longer than the Construction Period because orders typically incur costs earlier than when the actual construction begins.

