Accounting for Energy Credits & Other Intangible Certificates

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Agenda

1. What is a REC? SREC?
2. What other forms of similar attributes exist
3. Historical “GAAP”
4. Authoritative Guidance
5. Accounting Interpretations
6. Revenue & Expense Recognition, Valuation
7. Questions

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What is a REC?

A renewable energy credit.

It is a non-physical asset which can be separated from the actual kwh generated from a qualifying renewable energy source.

RECs generally exist to allow for generators to fulfill Renewable Portfolio Standards.

More details.

1 REC = 1mwh of energy from a renewable energy source.

RECs get their existence through typically a certification process in various energy markets or regions via a “minting” or “certification process”.

Some active markets exist for RECs depending on location.

Other Credits that Muddy the Water

SRECs – Solar Renewable Energy Credits

PTCs – Production Tax Credits

ITCs – Investment tax credits
Emission Credits (Allowances) – Allocated credits for carbon emissions management

These all tax different forms and are all very much different.

Differences

SRECs and RECs – generated from Mwh sales used to help subsidize out-of-market construction costs and support RPS standards.

ITCs and PTCs – used to reduce upfront construction costs by federally-taxed asset owners.

Emission Allowances – Required of generators of certain assets with carbon emissions.

This session deals with RECs and SRECs

Any public power utility that owns renewable energy assets such as wind or solar projects (and other types) will create RECs.

The growing relevance of solar has given rise to SRECs as well.

The distinction is only different in terms of the source of energy. Accounting and reporting is generally no different.

Generally Accepted Accounting Principles

The GAAP Hierarchy (GASB #76):

GAAP is defined as these two items:

GASB technical bulletins and AICPA guidance if approved by GASB

Everything else (only if it doesn't violate GAAP)

GAAP Guidance

Where to start?

1. What GASB guidance exists?
2. Any implementation guidance from GASB?

3. If not successful in #1 and #2, what should drive our position?

GASB guidance

No direct guidance exists for RECs. “You can’t be wrong” 

Where should we start to look? We can search for a correlation and can get to 3 potential areas:

1. Intangible Assets (GASB #51)
2. Inventory (GASB #34)
3. Investment Accounting (GASB #72/#31/#40)

Is a REC an intangible asset under GASB #51

Intent of GASB #51.   Internally created or purchased assets of non-physical nature.

Easements

Timber Rights

Internally created Software

GASB 51

If determined to be an “intangible asset” – it should be considered a capital asset subject to amortization.

How applicable does that sound for a REC used in the operating revenue process?

Reasonable Conclusion reached: GASB 51

It is a stretch (too big of a stretch) to consider a REC to be an intangible asset under GASB #51.

Nope……Don't use 51.

3.a. The provisions of this Statement apply to all intangible assets except for the following: Assets meeting the description [of an intangible asset]…..created primarily for the purpose of directly obtaining income[2]……..

[2.] The accounting and financial reporting for these assets generally follow authoritative guidance for investments. [GASB 31, 40, 72 perhaps].

Is a REC an investment?

Would a reasonable person determine that a REC is an investment similar to investment pools, cash, government securities, equities, or similar?

Reasonable conclusion: a REC is not an investment similar to what is generally understood to be investments for governments.

How about technical bulletins?

A search of the GASB implementation guide for any Q&A on “credits”.

Addresses emissions credits Z.51.37 - Treat emissions credits as zero basis (not on balance sheet). Record revenue upon sale.

Recap:

Now we conclude:

No direct GAAP guidance exists for reporting, recognition or valuation of RECs.

What would a reasonable approach look to be:

Accounting for RECs

Accounting for RECs should be an Accounting Policy decision made by the utility.

The policy should be reasonable and consistently applied with adequate disclosures made to financial statement readers, if material.

Establishing a Policy

1. What other information can I find to help?
2. What are other utilities doing?
3. Does FERC weigh in on this issue?

Let’s do some research and find a common approach.
Adopt that approach consistently.

Resources

Big 4 Research – Deloitte and PWC do a great job with public registrants

Best practices

Other regulatory agencies

Revenue and Expense Recognition

Revenues:

Determine when revenue should be recognized.

When is revenue created?   When kwh is generated? When the REC is certified?   When it is “sold”? What if its sold as part of a forward contract?

2 schools of thought:

1. REC is created when energy is generated.

2. REC is created upon asset transfer to a counter-party.

One is based on output and the other concludes that revenue can't be recognized until a "service has been rendered" or goods transfer. Both are appropriate if consistently applied.

REC created at generation

Record revenue as it is generated via two methods:

1. If under contract for sale, record at sale price.
2. If uncontracted, record as inventory and "Unbilled revenue" at expected sales price.

Adjustments can be made once actual REC is sold.

REC created at asset transfer

Record at asset transfer at agreed-upon price. No estimates made since sale won't take place until counterparty buys the REC.

If placed into a power market for sale, use most current auction prices.
Many times the REC owner will need to transfer ownership to the REC purchaser. Sale would take place at that time.

Should a REC be recognized as revenue when it is minted or certified?

Ask this question: Revenue is generally recognized when either 1. a service is rendered or 2. and asset is conveyed to the buyer.

Does either of these occur upon certification? Generally no.

Expense recognition

Follow the revenue.

Does it take any expenses to create a REC?

At generation: expense match revenue.

At sale: expense doesn't match revenue

Most consider the expense to create a REC as $0 anyway. We don't have any exposure to government utilities that allocate cost of a REC to inventory (out of power supply costs). But we do see this could be a reasonable approach.

Balance Sheet Impact

If RECs are sold at generation.

A/R	xxxxxxxx	
Sales		xxxxxx

Uncontracted RECs would be recorded as inventory at fair value.   Also, some can argue that inventory should be at LCM which equals zero.

If RECs are sold at asset transfer.   NO entry is made until transfer takes place.

What does FERC say?

FERC addresses allowances which is the closest applicability.

Record as inventory. If purchased with intent to resell, treat as investments.

This is only applicable if you file FERC reports which will create a different reporting basis than GAAP.

Overall.....

Select an accounting method that makes most appropriate sense for your utility.

Use it consistently and without bias.

Industry practices have adopted two primary methods while others do exist.

Be on the lookout for GASBs new revenue recognition guidance coming.

Questions.

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