AGENCY: Federal Energy Regulatory Commission.

ACTION: Notice of Proposed Rulemaking.

SUMMARY: The Federal Energy Regulatory Commission proposes to revise its regulations to update the accounting and reporting requirements under its Uniform Systems of Accounts for jurisdictional public utilities, natural gas companies and oil pipelines. The Commission proposes to establish uniform accounting requirements and related accounts for the recognition of changes in the fair value of certain security investments, items of other comprehensive income, derivative instruments, and hedging activities. The Commission proposes to add new balance sheet accounts to the Uniform Systems of Accounts to record items of other comprehensive income and derivative instruments. The Commission also proposes to add new general instructions and revise certain account instructions to incorporate the above changes in the existing Uniform Systems of Accounts.
Additionally, the Commission proposes to revise the following Annual Reports:

FERC Form No. 1, Annual Report of Major Public Utilities, Licensees and Others (Form 1); FERC Form No. 1-F, Annual Report of Nonmajor Public Utilities and Licensees (Form 1-F); FERC Form No. 2, Annual Report of Major Natural Gas Companies (Form 2); FERC Form No. 2-A, Annual Report of Nonmajor Natural Gas Companies (Form 2-A); and Form No. 6, Annual Report of Oil Pipeline Companies (Form 6) to include the new accounts and new schedules proposed by this rulemaking.

An important objective of the proposed rule is to provide sound and uniform accounting and financial reporting for the above types of transactions and events. The new instructions and accounts for recording the above transactions and events will result in improved, consistent and complete accounting and reporting. The addition of new accounts and new reporting schedule is intended to address and resolve the problems of lack of visibility, completeness and consistency of accounting and reporting changes in the fair value of certain financial instruments, items of other comprehensive income, derivative instruments and hedging activities, in the above mentioned FERC Forms.

COMMENT DATE: Comments on the proposed rulemaking are due on or before [insert date 60 days after publication in the FEDERAL REGISTER].

ADDRESS: File written comments with the Office of the Secretary, Federal Energy Regulatory Commission, 888 First Street, NE., Washington, D.C., 20426. Comments
should reference Docket No. RM02-3-000. Comments may be filed electronically or by paper (an original and 14 copies, with an accompanying computer diskette in the prescribed format requested).

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UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION  

Accounting and Reporting of Financial Instruments, Comprehensive Income, Derivatives and Hedging Activities  

Docket No. RM02-3-000  

NOTICE OF PROPOSED RULEMAKING  

(December 20, 2001)  

I. INTRODUCTION  

In this notice of proposed rulemaking (NOPR), the Federal Energy Regulatory Commission (Commission) proposes to amend its Uniform Systems of Accounts ¹ for public utilities and licensees² (public utilities), natural gas companies³ (gas companies)  

¹Section 301(a) of the Federal Power Act (FPA), 16 U.S.C. 825(a), section 8 of the Natural Gas Act (NGA), 15 U.S.C. 717g and section 20 of the Interstate Commerce Act (ICA), 49 App. U.S.C. 20 (1988), authorize the Commission to prescribe rules and regulations concerning accounts, records and memoranda as necessary or appropriate for the purposes of administering the FPA, NGA and the ICA. The Commission may prescribe a system of accounts for jurisdictional companies and, after notice and opportunity for hearing, may determine the accounts in which particular outlays and receipts will be entered, charged or credited.  


and oil pipeline companies \(^4\) (oil pipelines). Briefly, the Commission proposes to establish uniform accounting requirements for the recognition of changes in the fair value of certain security investments, items of other comprehensive income, derivative instruments, and hedging activities. The Commission proposes to add new balance sheet accounts to the Uniform Systems of Accounts to record items of other comprehensive income and changes in the fair value of derivative instruments. The Commission also proposes to add new general instructions for the accounting of derivative instruments and hedging activities along with new instructions for the accounting of items of other comprehensive income. Revisions to existing investment asset accounts and general instructions are proposed to incorporate fair value accounting for trading and available-for-sale type security investments.

Additionally, the Commission proposes to revise the following Annual Reports:

FERC Form No. 1, Annual Report of Major Public Utilities, Licensees and Others (Form 1); FERC Form No. 1-F, Annual Report of Nonmajor Public Utilities and Licensees (Form 1-F); FERC Form No. 2, Annual Report of Major Natural Gas Companies (Form 2); FERC Form No. 2-A, Annual Report of Nonmajor Natural Gas

Companies (Form 2-A); and Form No. 6, Annual Report of Oil Pipeline Companies (Form 6) to include the new accounts and a new schedule proposed by this rulemaking.\(^5\)

\(^5\)The FERC Annual Reports bear the following OMB approvals: Form No. 1 has OMB approval number 1902-0021; Form No. 1-F has OMB approval number 1902-0029; Form No. 2 has OMB approval number 1902-0028; Form No. 2-A has OMB approval number 1902-0030; and Form No. 6 has OMB approval number 1902-0022.
The purpose of the proposed rule is to provide useful financial information to regulatory agencies and other users of the financial statements of public utilities, gas companies and oil pipelines by establishing uniform accounting and reporting requirements for items of other comprehensive income, changes in the fair value of investment securities, derivatives, and hedging activities. An important objective of the proposed rule is to provide sound and uniform accounting and financial reporting for the above types of transactions and events. The Commission is of the view that such requirements are needed at this time because these types of transactions and events are not specifically addressed in the existing Uniform Systems of Accounts or in FERC Forms 1, 1-F, 2, 2-A, and 6. This NOPR is part of the Commission's ongoing effort to
address emerging accounting pronouncements within the context of the Uniform Systems of Accounts. 

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6On August 10, 2001, the Commission's Chief Accountant issued interim accounting guidance on the proper accounting and reporting requirements for changes in the fair value of certain investments in marketable securities, items of other comprehensive income, and derivatives and hedging activities. See, All Jurisdictional Public Utilities, Licensees, Natural Gas Companies, and Oil Pipeline Companies, 96 FERC & 62,147 (2001).
There are, however, a number of entities with market-based rates that have been exempted from the Commission's Uniform System of Accounts, and thus would not be subject to the proposed rule. For instance, Parts 41, 101, and 141 of the Commission's regulations prescribe certain informational requirements that focus on the assets that a public utility owns. For market-based applications, the Commission has taken the position that since a marketer does not own any electric power generation or transmission facilities, its jurisdictional facilities would be only corporate and documentary, its costs would be determined by utilities that sell power to it, and its earnings would not be defined and regulated in terms of an authorized return on invested capital, and that, accordingly, it would grant waivers to marketers of the requirements of these Parts. The Commission has also granted power marketers' requests for blanket approval under Part 34 of the Commission's regulations for all future issuances of securities and assumptions of liability, assuming that no party objects to such treatment during a notice period which the Commission provides.\(^7\) The purpose of section 204 of the Federal Power Act, which Part 34 implements, is to ensure the financial viability of public utilities obligated to

\(^7\)We note that the Commission's jurisdiction over issuances of securities and assumptions of liabilities under section 204 of the FPA applies only to entities that are public utilities as defined in the FPA and only where the public utilities' security issues are not regulated by a State commission (see FPA section 204(f)).
serve electric consumers. The Commission concluded that since marketers do not obligate themselves to serve electric consumers, the requirements are inapplicable.\(^8\)

As the development of competitive wholesale power markets continues, however, independent and affiliated power marketers and power producers are playing more significant roles in the electric power industry. In light of the evolving nature of the electric power industry, the Commission seeks comment on the extent to which these entities should be required to follow the Uniform System of Accounts, what financial information, if any, should be reported by these entities, how frequently it should be reported, and, in particular, whether these exempted entities should be subject to

reporting the information required in the proposed regulations. Furthermore, the Commission seeks comments on whether we should rescind the Part 34 blanket authorizations granted to these entities and require these entities to comply with the filing requirement of Part 34 for all future issuances of securities and assumptions of liabilities.

Finally, the proposed rule is not intended to prescribe the ratemaking treatment for items of other comprehensive income or for derivative instruments and hedging activities. The Commission's proposal does not bar regulatory commissions (including this Commission) from adopting any particular ratemaking treatment for these transactions.

II. BACKGROUND

A. General

In recent years, fair value measurements have become useful in assisting investors, creditors and other users of the financial data in making rational investment, credit and similar decisions. The use of fair value as a measurement attribute for financial reporting has grown in importance and relevance. Despite this fact, the companies that this Commission regulates have had only a relatively small number of transactions for which fair value measurements would be appropriate. This however is changing. As the regulated industries restructure, fair value will provide a relevant measure of economic effects for a growing number of transactions and events. The potential usefulness of fair value information has resulted in the Financial Accounting Standards Board (FASB)\(^9\)

\(^9\)FASB and other accounting bodies are responsible for establishing and improving
issuing new accounting pronouncements affecting the manner in which certain types of financial instruments, derivatives and hedging activities are measured and reported in the financial statements applicable to entities in general.\textsuperscript{10}

\textsuperscript{10}The accounting pronouncements issued by FASB were Financial Accounting Standards (FAS) 115, Accounting for Certain Investments in Debt and Equity Securities, 130, Reporting Comprehensive Income, and 133, Accounting for Derivative Instruments and Hedging Activities, as amended by 138, Accounting for Certain Derivative Instruments and Certain Hedging Activities. These accounting pronouncements may be obtained from FASB at ( http://accounting.rutgers.edu/raw/fasb/ ).
The Commission considers the requirements contained in Financial Accounting Standards (FAS) 115, 130 and 133 to be an improvement in financial accounting and reporting practices if properly implemented. Also, as a general proposition, the Commission considers it desirable for its accounting requirements and those used for general purpose financial reporting to be consistent. While some companies have implemented certain aspects of these pronouncements, the implementation has not been uniform concerning the accounting and reporting to the Commission in the FERC Forms 1, 1-F, 2, 2-A, and 6. Therefore the Commission plans to implement the principles and concepts set forth in FAS 115, 130 and 133 for FERC accounting and reporting purposes effective upon the issuance of a final order in this proceeding. Consequently, the interim accounting and reporting guidance provided by the Chief Accountant on August 10, 2001, will be superceded with the issuance of the final rule in this proceeding.\(^{11}\)

In summary, the Commission considers that the proposed accounting and reporting changes will provide consistent accounting and reporting of changes in the fair value of financial investments, derivatives and hedging activities. The proposed changes will also minimize the accounting and reporting burden on jurisdictional entities and assist the Commission in its analysis of profitability, efficiency, risk management, and in its overall monitoring effort.

\(^{11}\)See note 6.
In order to provide a context for the Commission's proposed changes the key aspects of the relevant FASB pronouncements are provided below.

**B. Investments in Debt and Equity Securities**

In May 1993, the FASB issued Financial Accounting Standard (FAS) 115, Accounting for Certain Investments in Debt and Equity Securities, effective for fiscal years beginning after December 15, 1993. This statement addresses the accounting and reporting for investments in equity securities that have readily determinable fair value and for all investments in debt securities.

This accounting pronouncement requires entities to classify investments in securities into one of three categories, held-to-maturity, trading, or available-for-sale.

The first category of investments, held-to-maturity, consists of debt securities that the entity has the intent and ability to hold to maturity. For debt securities held to maturity, the cost will be the amount realized when the entity redeems the security. Therefore, changes in the fair value of securities held to maturity are not recognized during the period the entity holds the security investment.

Securities that fall into the second category, trading type securities, reflect active and frequent buying and selling. They are held for short periods of time with the objective of generating profits from short term differences in price. Entities must recognize unrealized holding gains and losses on trading type securities in earnings when the fair value of security changes.
Securities that do not fall into the category of held-to-maturity or trading type securities are considered to be available-for-sale. Changes in the fair value of available for sale type securities are reflected in the financial statements in "other comprehensive income" rather than earnings. This accounting treatment results in unrealized holding gains and losses on debt and equity securities that are available for sale being reported outside of earnings because they are not actively managed in a trading account.

C. Other Comprehensive Income

In June 1997, the FASB issued FAS 130, Reporting Comprehensive Income. This statement established the standards for reporting comprehensive income in a full set of general-purpose financial statements effective for fiscal years beginning after December 15, 1997. Comprehensive income represents the change in equity of an entity during a period from transactions and other events and circumstances from nonowner sources. Comprehensive income is composed of traditional net income plus items of "other comprehensive income."  

12 Comprehensively income is defined by FASB in Concepts Statement No. 6 as, "the change in equity [net assets] of a business enterprise during a period from transactions and other events and circumstances from nonowner sources. It includes all changes in equity during a period except those resulting from investments by owners and
Items of other comprehensive income are amounts under existing accounting standards that were permitted to bypass the income statement and be recorded directly in a separate section of equity. These amounts were required to be classified by their category and reported separately from retained earnings and additional paid-in capital. Under existing accounting standards other comprehensive income categories include, foreign currency items, minimum pension liability adjustments, unrealized gains and losses on certain investments in debt and equity securities, and cash flow hedge amounts.

Under the provision's of FAS 130, entities may report the categories of other comprehensive income using an income statement format or by showing the amounts as part of the Statement of Shareholders Equity. Entities may also report the amounts on a before-tax or after-tax basis provided that certain disclosures are made in the notes to the financial statements.

D. Derivative Instruments and Hedging Activities

1. General

In June 1998, the FASB issued FAS No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended on June 2000, by FAS 138, Accounting for Certain Derivative Instruments and Certain Hedging Activities. This pronouncement was issued in a response to an increased use of derivatives and to resolve problems with the accounting and reporting practices for derivatives and hedging activities. These problems included incomplete and inconsistent accounting guidance on the effects of derivative transactions and hedging activities. The effects of derivatives were not
transparent in the basic financial statements, and many derivative instruments were
carried "off-balance-sheet" regardless of whether they were formally part of a hedging
strategy. The FASB issued new accounting guidance to address these concerns.

2. **Definition of a Derivative**

   A derivative instrument is defined for accounting purposes based on its
distinguishing characteristics rather than by specific examples of derivative instruments
such as futures or option contracts because the expansion of financial markets and other
contracts could ultimately render obsolete a definition based solely on examples.

   A derivative instrument is a financial instrument or other contract with all of the
following characteristics:

   First, the instrument has one or more underlyings. An underlying is a specified
interest rate, security price, commodity price, foreign exchange rate, index of prices or
rates, or other variable. An underlying may be a price or rate of an asset or liability but is
not the asset or liability itself.

   Second, the instrument must have one or more notional amounts or payment
provisions. A notional amount represents quantity such as a number of currency units,
shares, bushels, pounds or other units specified in a derivative instrument. Those terms
determine the amount of the settlement or settlements, and, in some cases, whether or not
a settlement is required.
Third, the instrument requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have similar response to changes in market factors.

Finally, the instrument requires or permits net settlement. It can readily be settled net by a means outside the contract, or it provides for delivery of an asset that puts the recipient in a position not substantially different from net settlement.

Certain types of contracts are exempted from the requirements of this statement. For example, normal purchases and normal sales contracts that provided for the purchase or sale of goods that will be delivered in quantities expected to be used or sold by the reporting entity over a reasonable period in the normal course of business are not considered derivative instruments. This exception is commonly referred to as the normal purchases and normal sales scope exception. The exception would include typical purchases and sales of inventory items, certain insurance contracts, and employee compensation agreements. Derivative instruments that do not qualify for the normal purchases and normal sales scope exception, or other exceptions provided for under the statement, are reflected in the financial statements. Consequently, most futures, forwards, swaps, and option contracts meet the definition of a derivative instrument and changes in their fair value would be reflected in the financial statements.

3. **Accounting for a Derivative Instrument**

Changes in the fair value of derivative instruments depends upon its intended use and designation. Essentially, entities recognize in earnings in the period of the change
gains or losses on certain derivative instruments not designated as a hedge instrument. The change in the value of the derivative instrument is reflected on the balance sheet as an asset or liability with a corresponding amount recognized in earnings. This accounting effectively provides users of the financial statements with information concerning the value of the derivative instrument as if it had been settled in the market place.

4. **Hedge Accounting**

Providing certain criteria are met, a derivative may be specifically designated as a fair value or cash flow hedge. Entities hedge to manage risk to prices, interest rates, or foreign currency exposures. Under the rules for hedge accounting the changes in the fair value of the derivative are measured at fair value with adjustments made to the carrying amount of the items being hedged (as in a fair value hedge) or to other comprehensive income (as in a cash flow hedge) to the extent the hedge is effective.

a. **Fair Value Hedge**

In a fair value hedge a derivative instrument is designated as a hedge against exposure to changes in the fair value of a recognized asset, liability, or a firm commitment. A firm commitment is defined as an agreement with an unrelated party, binding on both parties and usually legally enforceable. The agreement specifies all significant terms, including the quantity to be exchanged, the fixed price, and the timing
of the transaction. The fixed price may be expressed as a specified amount of an entity's functional currency or a foreign currency. It may also be expressed as a specified interest rate or specified effective yield.

In a fair value hedge, the change in value of the derivative instrument is recognized in earnings in the period of the change together with the offsetting gain or loss on the item being hedged. To the extent that a hedge is perfectly effective, it will produce the same offsetting amounts in earnings so that net income is not impacted by the hedge. However, amounts would be reflected in earnings to the extent that the hedge is not effective in offsetting the change in value of the item being hedged.

Additionally, fair value hedge accounting results in an adjustment of the carrying amount of the hedged asset or liability. In the case of a fair value hedge of a firm commitment, a new asset or liability is created. As a result of the hedge relationship, the new asset or liability ultimately becomes part of the carrying amount of the item being hedged.

b. Cash Flow Hedge

A cash flow hedge uses a derivative instrument to protect against the risk caused by variable prices or costs, that cause future cash flows to be uncertain. It is a hedge against an anticipated or forecasted transaction that is probable of occurring in the future but the amount of the transaction has not been fixed.

In a cash flow hedge, the effective portion of the derivative's gain or loss is initially reported as a component of other comprehensive income. The ineffective portion
of the gain or loss is reported in earnings immediately. Amounts recorded in other comprehensive income are reclassified into earnings when the hedged item affects earnings.

c. **Documentation of Hedge Relationship**

Entities must keep extensive documentation of the hedge relationship. An entity that elects to apply the special hedge accounting is required to document at the inception of the hedge the risk management objective and strategy for undertaking the hedge, including the hedge instrument, the related transaction, the nature of the risk being hedged, and how hedge effectiveness will be determined.

The company's documentation of its overall risk management philosophy is essential in addressing the role that derivative instruments and hedging activities play in achieving the company's risk management objectives.

Concurrent designation and documentation of a hedge is critical because an entity could retroactively identify a transaction as a hedge or change a method of measuring effectiveness to achieve a desired outcome. At the inception of the hedge formal documentation is required that identifies the hedging instrument and specifically identifies the hedged item or transaction along with the nature of the risk being hedged. Entities are required to formally document how effectiveness will be assessed at the adoption of the hedge and on an ongoing basis.

**III. DISCUSSION**

**A. General**
The Commission's existing Uniform Systems of Accounts for public utilities, gas companies and oil pipelines do not specifically address the proper accounting and reporting for changes in the fair value of certain investment securities, derivative instruments, and hedging activities. Additionally, the existing Uniform Systems of Accounts do not contain specific accounts to record amounts related to items of other comprehensive income or a format to display comprehensive income in the FERC Forms 1, 1-F, 2, 2-A, and 6.

Without specific instructions and accounts for recording and reporting the above transactions and events, inconsistent and incomplete accounting will result. For example, if the effects of certain derivative instruments and hedging activities are not properly reported to the Commission in the FERC Annual Reports, it will be difficult for the Commission and others to determine the extent and effects of derivatives on a jurisdictional entity's financial statements and results of operations. The addition of new accounts and related general instructions is intended to improve the visibility, completeness and consistency of accounting and reporting of changes in the fair value of certain investment securities, items of other comprehensive income, derivatives and hedging activities.

Also, the addition of the proposed new accounts and related reporting requirements to the FERC Forms 1, 1-F, 2, 2A and 6 will reduce regulatory uncertainty as to the proper accounting and reporting for these items and minimize regulatory burden by reducing the potential differences in the manner in which these amounts are reported to
shareholders and to the Commission. Finally, the reporting of derivatives and hedging activities by jurisdictional entities will assist the Commission in its analysis of profitability, efficiency, risk and in its overall monitoring effort.

B. Proposed Accounting for Trading and Available-for-Sale Type Securities

Under the Commission's Uniforms Systems of Accounts for public utilities and gas companies, all types of securities are recorded at cost and subsequent changes in the fair value of security investments are not recognized in the financial statements. The Uniform System of Accounts for oil pipelines requires adjustments to the carrying value of security investments when certain conditions are met.

The Commission is of the view that fair value measurement of the trading and available-for-sale type securities presents relevant and useful information to existing and potential investors, creditors, regulators and others in making credit and other decisions. Fair value measurements will also provide useful information to the Commission concerning the status of certain amounts set aside to fund future obligations.

The Commission therefore proposes to add language to its security investment accounts for public utilities, gas companies, and oil pipelines to permit the recognition of changes in the fair value of trading and available-for-sale types of securities due to unrealized holding gains and losses. The Commission also proposes amending its oil

13 The security investment accounts for public utilities and gas pipeline companies
pipeline General Instruction 1-15, Accounting for marketable equity securities, and remove oil pipeline Accounts 23, 24, and 75.5 to conform the regulations to the proposed changes.

C. Proposed Accounting for Other Comprehensive Income

As part of the proposed rule, the Commission proposes to revise the Uniform Systems of Accounts for public utilities, gas companies and oil pipelines to provide accounting for items of other comprehensive income. As proposed, new equity Account 219, Accumulated other comprehensive income, would be created for public utilities and gas companies, and a new equity Account 77, Accumulated other comprehensive income, are: Account 124, Other investments; Account 125, Sinking funds (Major only); Account 126, Depreciation fund (Major only); Account 127, Amortization fund (Major only); Account 128, Other special funds (Major only); and Account 129, Special funds (Nonmajor only). The security investment asset accounts for oil pipelines are Account 11, Temporary investments; Account 21, Other investments; and Account 22, Sinking and other funds.
would be established for oil pipelines to include the accumulated balance for items of other comprehensive income. The accounts will require supporting records be maintained by each category of other comprehensive income for reporting the information in the FERC Form 1, 1F, 2, 2A, and 6.

As proposed, a new equity account entitled Account 219.1, Other comprehensive income, for public utilities and gas companies, and a new account entitled Account 77.1, Other comprehensive income, for oil pipeline companies, would be established to include amounts for items of other comprehensive income for the reporting year. The purpose of these accounts is to record the activity for items of other comprehensive income during the year. At year end, the amounts recorded in Account 219.1 and Account 77.1 would be transferred to the new equity Account 219 and Account 77, respectively. Consequently, Accounts 219.1 and 77.1 as proposed will always have a zero beginning and year end balance and therefore the Commission proposes not to include these accounts as part of the balance sheet schedules. Accounts 219.1 and 77.1 will capture activity during the year for items of other comprehensive income and the activity will be reported in a proposed new schedule entitled "Statement of Comprehensive Income and Hedging Activities."

The proposed instructions to the other comprehensive income accounts for all jurisdictional entities will require that supporting records be maintained by each category of other comprehensive income. This level of detail is required so that the entity is able
to identify the amounts associated with the item when it enters into the determination of earnings in current or subsequent periods.

Finally, reclassification adjustments are required to be made for items of other comprehensive income to avoid double counting an item in net income and other comprehensive income. The proposed instructions to Accounts 219 and 219.1 for public utilities and natural gas companies, and the proposed instructions to Accounts 77 and 77.1 for oil pipeline companies will require that reclassification adjustments be made directly to these accounts as appropriate. This proposed accounting treatment for reclassification adjustments will minimize the need for creating a new account to capture amounts solely related to reclassification adjustments.

D. Proposed Accounting for Derivatives and Hedging Activities

1. General

The Commission’s existing Uniform Systems of Accounts for public utilities, natural gas companies and oil pipelines do not contain specific accounts to record changes in the fair value of derivative instruments used in hedging and non-hedging activities. The Commission considers that the addition of new accounts and instructions will provide improved visibility, and completeness of accounting and reporting of derivatives and hedging activities by jurisdictional entities. As part of the proposed rule,
the Commission proposes to revise the Uniform Systems of Accounts to provide accounting for derivatives and hedging activities.

2. **Proposed General Instructions for Fair Value and Cash Flow Hedges**

   The Commission proposes to add a new general instruction that would require public utilities, natural gas companies, and oil pipelines to record changes in the fair value of the derivative instrument designated as a cash flow hedge to other comprehensive income. The ineffective portion of the cash flow hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of, or otherwise settled.

   The proposed instructions would also require jurisdictional entities to record changes in the fair value of a derivative instrument designated as a fair value hedge in this account with a concurrent charge to a subaccount of the asset or liability that carries the item being hedged. The ineffective portion of the fair value hedge would be charged to the same income or expense account that would have been used if the hedged item had been disposed of, or otherwise settled.

3. **Proposed Changes to General Instruction 21. Allowances**

   The Commission is also proposing to make technical changes to its existing general instructions concerning the accounting for hedge transactions related to exchange traded allowance future contracts. General Instruction No. 21. Allowances, of Part 101, directs public utilities to defer in Account 186, Miscellaneous deferred debits, or Account 253, Other deferred credits, the costs and benefits from hedging transactions
associated with exchange traded allowance future contracts. The Commission is proposing to delete paragraph I to be consistent with proposed accounting for derivatives.

The accounting framework proposed for derivatives would also include exchange traded future allowances.

4. Proposed Accounting for Derivative Assets and Liabilities

As proposed, two new asset and two new liability accounts would be established to include amounts related to the changes in the fair value of derivative instruments not designated as a cash flow or fair value hedges. The two new asset accounts are Account 175, Derivative instrument assets, for public utilities and natural gas companies, and Account 46, Derivative instrument assets, for oil pipeline companies. The two new liability accounts are Account 244, Derivative instrument liabilities, for public utilities and natural gas companies, and Account 65, Derivative instrument liabilities, for oil pipeline companies.

Public utilities and natural gas companies would charge Account 421, Miscellaneous nonoperating income, with the corresponding amount of the change in the fair value of the derivative instruments. Oil pipelines would charge Account 660, Miscellaneous income charges, with the corresponding amount of the change in the fair value of the derivative instruments.

The Commission recognizes that under certain circumstances rate regulators may include all or part of a derivative instruments change in value in the development of rates even though the derivative instrument is not part of a fair value or cash flow hedge. The
Commission therefore proposes where regulators explicitly approve the inclusion of the changes in fair value of derivative instruments in the development of rates, company's will reclassify those amounts from Account 421 or Account 660 to the appropriate utility operating revenue or expense account that will be charged with the transaction when it settles.

The Commission also recognizes that companies are required to classify derivative asset and liabilities as current or long-term on their balance sheets. In order to facilitate reporting derivative asset and liabilities to shareholders in general purpose financial statements, companies may create current and long-term subaccounts associated with the proposed new derivative balance sheet accounts.

Finally, if the derivative instrument does not qualify for hedge accounting, but it is probable that the rate regulator will include the changes in the fair value of the derivative instrument in the future development of rates, the entity must follow the Commission's existing accounting regulations for the recognition of regulatory assets and regulatory liabilities.

5. **Proposed Accounting for Fair Value and Cash Flow Hedges**

As proposed, two new asset and two new liability accounts would be established to include amounts related to the changes in the fair value of derivative instruments designated as a cash flow or fair value hedges. The two new asset accounts are Account 176, Derivative instrument assets-Hedges, for public utilities and natural gas companies, and Account 47, Derivative instrument assets-Hedges, for oil pipelines. The two new
liability accounts are Account 245, Derivative instrument liabilities-Hedges, for public utilities and natural gas companies, and Account 66, Derivative instrument liabilities-Hedges, for oil pipelines.

**E. Proposed Changes to the FERC Annual Reports Forms**

The proposed accounting changes, if adopted, will require one new schedule and changes to existing balance sheet schedules in the FERC Forms 1, 1-F, 2, 2-A, and 6 filed with the Commission by public utilities, gas companies, and oil pipelines. The proposed new schedule is attached in Appendix A and the proposed changes to the FERC Forms are discussed below.

As previously mentioned, entities have a choice of formats for their general purpose financial statements along with a choice of reporting certain items net of reclassification adjustments and a choice of reporting these amounts on a net-of-tax or pre-tax basis provided that certain footnote disclosure requirements are met. In order to provide consistent accounting and reporting of items of other comprehensive income the Commission is adding a new schedule entitled "Statement of Comprehensive Income and Hedging Activities" with instructions on the proper footnote disclosures for the FERC Forms 1, 1-F, 2, 2-A, and 6.

This proposed new schedule is modeled after an income statement approach which provides the most transparency for the components of other comprehensive income and is more consistent with the overall framework of the FASB Concepts Statements. The proposed income statement format would also avoid duplication of data already reported
on other schedules. This new schedule will show the components of other comprehensive income and require:

(1) the reporting of categories of other comprehensive income on a net-of-tax basis, where appropriate, along with the reporting of the related tax effects allocated to each component, in a footnote to the schedule.

(2) the reporting of accumulated other comprehensive income balances at year end by category, in a footnote to the schedule.

(3) the reporting of fair value hedge balances at year end by category, in a footnote to the schedule.

The Commission concludes that the above reporting requirements would not be a significant reporting burden to industry since the information is already being captured by their accounting systems for internal and external reporting as needed.

IV. REGULATORY FLEXIBILITY ACT STATEMENT

The Regulatory Flexibility Act (RFA) requires agencies to prepare certain statements, descriptions, and analyses of proposed rules that will have a significant economic impact on a substantial number of small entities.\(^{14}\) The Commission is not required to make such analyses if a rule would not have such an effect.

The Commission concludes that this rule would not have such an impact on small entities. Most filing companies regulated by the Commission do not fall within the

RFA's definition of a small entity.\textsuperscript{15} As previously mentioned, the Commission concludes that this reporting would not be a significant burden to industry since the information is already being captured by their accounting systems and generally being reported to shareholders and others at a company, or at a consolidated business level. However, if the reporting requirements represent an undue burden on small businesses, the entity affected may seek a waiver of the disclosure requirements from the Commission.

V. ENVIRONMENTAL IMPACT STATEMENT

The Commission excludes certain actions not having a significant effect on the human environment from the requirement to prepare an environmental assessment or an

\textsuperscript{15} 5 U.S.C. 601(3), citing to section 3 of the Small Business Act, 15 U.S.C. 632. Section 3 of the Small Business Act defines a "small-business concern" as a business which is independently owned and operated and which is not dominant in its field of operation.
environmental impact statement.\textsuperscript{16} No environmental consideration is raised by the promulgation of a rule that is procedural or does not substantially change the effect of legislation or regulations being amended.\textsuperscript{17} The proposed rule updates the Parts 101, 201 and 352 of the Commission's regulations, and does not substantially change the effect of the underlying legislation or the regulations being revised or eliminated. Accordingly, no environmental consideration is necessary.

\textbf{VI. INFORMATION COLLECTION STATEMENT AND PUBLIC REPORTING BURDEN}

The following collections of information contained in this proposed rule have been submitted to the Office of Management and Budget (OMB) for review under '3507(d) of the Paperwork Reduction Act of 1995, 44 U.S.C. 3507(d). Comments are solicited on the Commission's need for this information, whether the information will have practical utility, the accuracy of provided burden estimates, ways to enhance the

\textsuperscript{16} 18 CFR 380.4.

\textsuperscript{17} 18 CFR 380.4(a)(2)(ii).
quality, utility, and clarity of the information to be collected, and any suggested methods for minimizing respondent's burden, including the use of automated information techniques.

*Estimated Annual Burden:*

The Commission estimates that on average it will take respondents 2 hours to comply with the proposed requirements. This will result in total hours for the following collections of information:

<table>
<thead>
<tr>
<th>Data Collection</th>
<th>No. of Respondents</th>
<th>No. of Responses</th>
<th>Total Annual Hours</th>
</tr>
</thead>
<tbody>
<tr>
<td>FERC-Form 1</td>
<td>210</td>
<td>210</td>
<td>420</td>
</tr>
<tr>
<td>FERC Form 1-F</td>
<td>7</td>
<td>7</td>
<td>14</td>
</tr>
<tr>
<td>FERC Form 2</td>
<td>57</td>
<td>57</td>
<td>114</td>
</tr>
<tr>
<td>FERC Form 2-A</td>
<td>57</td>
<td>57</td>
<td>114</td>
</tr>
<tr>
<td>FERC Form 6</td>
<td>159</td>
<td>159</td>
<td>318</td>
</tr>
<tr>
<td>Totals</td>
<td></td>
<td></td>
<td>980</td>
</tr>
</tbody>
</table>

*Total Annual Hours for Collection:*

(Reporting + Recordkeeping, (if appropriate)) = 980 + 470 hours* (recordkeeping)
=1,450 hours.

*This estimate is based on an average of 3 hours per respondent for recordkeeping purposes.

Information Collection Costs: The Commission seeks comments on the costs to comply with these requirements. It has projected the cost for complying to be the following: 1,450 hours \( \div 2,080 \times $117,041 = $81,596. \)

<table>
<thead>
<tr>
<th>Annualized Capital/Startup Costs</th>
<th>$ 0</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annualized Costs (Operations &amp; Maintenance).</td>
<td>$ 81,596</td>
</tr>
<tr>
<td>Total Annualized Costs</td>
<td>$ 81,596</td>
</tr>
</tbody>
</table>

OMB’s regulations require it to approve certain information collection requirements imposed by agency rule. The Commission is submitting notification of this proposed rule to OMB.\(^{18}\)

*Title:* FERC Form 1 Annual Report of Major Electric Utilities, Licensees and Others;

FERC Form 1-F Annual Report For Non-Major Public Utilities and Licensees;

FERC Form 2 Annual Report for Major Natural Gas Companies;

\(^{18}\)5 CFR 1320.11.
FERC Form 2-A Annual Report for Nonmajor natural gas companies;
FERC Form No. 6 Annual Report of Oil Pipeline Companies.

Action: Proposed Collections

OMB Control No: 1902-0021; 1902-0029; 1902-0028; 1902-0030; and 1902-0022.

Respondents: Business or other for profit.

Frequency of Responses: Annual.

Necessity of the Information: The Commission's existing Uniform Systems of Accounts do not specifically address the proper accounting and reporting for changes in fair value of certain investment securities, and derivative instruments and hedging activities. Additionally, the existing Uniform Systems of Accounts do not contain specific accounts to record amounts related to items of other comprehensive income in its annual financial reports.

Without specific instructions and accounts for recording and reporting the above transactions and events, inconsistent and incomplete accounting will result. The addition of new accounts and related general instructions is intended to improve the visibility, completeness and consistency of accounting practices for derivative instruments and hedging activities, and items of other comprehensive income.

As these derivative instruments are risk-shifting devices, it is important to identify and fully comprehend the risks being assumed, evaluate those risks and continuously monitor and manage those risks. Part of the risk identification process is a determination of the monetary exposure of the parties under the terms of the derivative instrument. In a
derivative situation, performance of the other party's obligations is highly dependent on the strength of its balance sheet.

Internal Review: The Commission has reviewed the requirements pertaining to the Uniform Systems of Accounts and to the financial reports it prescribes and determined the proposed revisions are necessary because the Commission needs to establish uniform accounting and reporting requirements for items of other comprehensive income, changes in the fair value of investment securities and derivatives, and hedging activities.

These requirements conform to the Commission's plan for efficient information collection, communication, and management within the electric, natural gas and oil pipeline industries. The Commission has assured itself, by means of internal review, that there is specific, objective support for the burden estimates associated with the information requirements.

Interested persons may obtain information on the reporting requirements by contacting the following: Federal Energy Regulatory Commission, 888 First Street, NE, Washington, DC 20426, [Attention: Michael Miller, Office of the Chief Information Officer, Phone: (202)208-1415, fax: (202)208-2425, e-mail: mike.miller@ferc.fed.us]

For submitting comments concerning the collections of information and the associated burden estimate(s), please send your comments to the contact listed above and to the Office of Management and Budget, Office of Information and Regulatory Affairs, 725 17th Street, NW, Washington, DC 20503 [Attention: Desk Officer for the Federal
VII. PUBLIC COMMENT PROCEDURES

The Commission invites all interested persons to submit comments on this NOPR.

To facilitate the Commission's review of comments, commenters are requested to provide an executive summary of their position on the issues raised in the NOPR. Commenters are requested to identify each specific question posed by the NOPR that their discussion addresses and to use appropriate heading. Additional issues the commenters wish to raise should be identified separately. The commenters should double space their comments.

Comments may be filed paper or electronically via the Internet and must be received by the Commission within 60 days after publication in the Federal Register. Those filing electronically do not need to make a paper filing. For paper filings, the original and 14 copies of such comments should be submitted to the Office of the Secretary, Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, DC 20426 and should refer to Docket No. RM02-3-000.

Comments filed via the Internet must be prepared in WordPerfect, MS Word, Portable Document Format, or ASCII format. To file the document, access the Commission's website at www.ferc.gov and click on "e-Filing," and then follow the instructions on each screen. First time users will have to establish a user name and
password. The Commission will send an automatic acknowledgment to the sender's E-Mail address upon receipt of comments.

User assistance for electronic filing is available at 202-208-0258 or by E-Mail to efiling@ferc.fed.us. Comments should not be submitted to the E-Mail address. All comments will be placed in the Commission's public files and will be available for inspection in the Commission's Public Reference Room at 888 First Street, N.E., Washington D.C. 20426, during regular business hours. Additionally, all comments may be viewed, printed, or downloaded remotely via the Internet through FERC's Homepage using the RIMS link. User assistance for RIMS is available at 202-208-2222, or by E-Mail to RimsMaster@ferc.fed.us.

III. DOCUMENT AVAILABILITY

In addition to publishing the full text of this document in the Federal Register, the Commission also provides all interested persons an opportunity to view and/or print the contents of this document via the Internet through FERC's Home Page (http://www.ferc.fed.gov) and in FERC's Public Reference Room during normal business hours (8:30 a.m. to 5:00 p.m. Eastern time) at 888 First Street, N.E., Room 2A, Washington, DC 20426.

From FERC's Home Page on the Internet, this information is available in both the Commission Issuance Posting System (CIPS) and the Records and Information Management System (RIMS).
CIPS provides access to the text of formal documents issued by the Commission since November 14, 1994.

B CIPS can be accessed using the CIPS link or the Energy Information Online icon. The full text of this document is available on CIPS in ASCII and WordPerfect 8.0 format for viewing, printing, and/or downloading.

RIMS contains images of documents submitted to and issued by the Commission after November 16, 1981. Documents from November 1995 to the present can be viewed and printed from FERC's Home Page using the RIMS link or the Energy Information Online icon. Descriptions of documents back to November 16, 1981, are also available from RIMS-on-the-Web; request for copies of these and other older documents should be submitted to the Public Reference Room.

User assistance is available for RIMS, CIPS, and the Website during normal business hours from our Help line at (202) 208-2222 (E-Mail to WebMaster@ferc.fed.us) or the Public Reference Room at (202) 208-1371 (E-Mail to public.referenceroom@ferc.fed.us).

During normal business hours, documents can also be viewed and/or printed in FERC's Public Reference Room, where RIMS, CIPS, and FERC Website are available. User assistance is also available.

List of Subjects
Docket No. RM02-3-000

18 CFR Part 101

Electric power, Electric utilities, Reporting and recordkeeping requirements, Uniform System of Accounts

18 CFR Part 201

Natural gas, Reporting and recordkeeping requirements, Uniform System of Accounts

18 CFR Part 352

Pipelines, Reporting and recordkeeping requirements, Uniform System of Accounts

By direction of the Commission.

(SEAL)

Linwood A. Watson, Jr.,
Acting Secretary.
ATTACHMENT NOT ON DISKETTE. COPIES WILL BE AVAILABLE IN RIMS AND THE PUBLIC REFERENCE ROOM.
In consideration of the foregoing, the Commission proposes to amend Parts 101, 201, and 352, Title 18 of the Code of Federal Regulations, as follows:

**PART 101B UNIFORM SYSTEM OF ACCOUNTS PRESCRIBED FOR PUBLIC UTILITIES AND LICENSEES SUBJECT TO THE PROVISIONS OF THE FEDERAL POWER ACT**

1. The authority citation for part 101 continues to read as follows:


2. In part 101, General Instructions, 21. Allowances., paragraph I is removed, and General Instructions 23. Accounting for other comprehensive income., and 24. Accounting for derivative instruments and hedging activities., are added to read as follows:

   **General Instructions**

   * * * * * * *

   23 Accounting for other comprehensive income.

   (A) Utilities will record items of other comprehensive income in account 219.1, Other comprehensive income. Amounts included in this account will be maintained by each category of other comprehensive income. Examples of categories of other comprehensive income include, foreign currency items, minimum pension liability adjustments, unrealized gains and losses on available-for-sale type securities and cash flow hedge amounts.
(B) At year end, amounts recorded in account 219.1, Other comprehensive income, will be transferred to account 219, Accumulated other comprehensive income. Supporting records will be maintained for account 219 so that the company can readily identify the cumulative amount of other comprehensive income for each item included in this account.

(C) When an item of other comprehensive income enters into the determination of earnings in the current or subsequent periods, a reclassification adjustment will be recorded in accounts 219 or 219.1 to avoid double counting of that amount.

24 Accounting for derivative instruments and hedging activities.

A. Utilities will recognize derivative instruments as either assets or liabilities in the financial statements and measure those instruments at fair value. A derivative instrument is a financial instrument or other contract with all of the following characteristics:

1. It has one or more underlyings and a notional amount or payment provision. Those terms determine the amount of the settlement or settlements, and, in some cases, whether or not a settlement is required.

2. It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors.
3. Its terms require or permit net settlement, can readily be settled net by a means outside the contract, or provides for delivery of an asset that puts the recipient in a position not substantially different from net settlement.

B. The accounting for the changes in the fair value of derivative instruments depends upon their intended use and designation. Changes in the fair value of derivative instruments not designated as fair value or cash flow hedges will be recorded in account 175, Derivative instrument assets, or account 244, Derivative instrument liabilities, as appropriate, with the gains or losses charged to earnings in account 421, Miscellaneous nonoperating income.

C. A derivative instrument may be specifically designated as a fair value or cash flow hedge. A hedge is used to manage risk to price, interest rates, or foreign currency transactions. A company will maintain documentation of the hedge relationship at the inception of the hedge that details the risk management objective and strategy for undertaking the hedge, the nature of the risk being hedged, and how hedge effectiveness will be determined.

D. If the utility designates the derivative instrument as a fair value hedge against exposure to changes in the fair value of a recognized asset, liability, or a firm commitment, it will record the change in fair value of the derivative instrument to account 176, Derivative instrument assets-Hedges, or account 245, Derivative instrument liabilities-Hedges, as appropriate, with a corresponding adjustment to the subaccount of the item being hedged. The ineffective portion of the hedge transaction will be reflected
in the same income or expense account that would have been used if the hedged item had been disposed of or settled. In the case of a fair value hedge of a firm commitment a new asset or liability is created. As a result of the hedge relationship, the new asset or liability will become part of the carrying amount of the item being hedged.

E. If the utility designates the derivative instrument as a cash flow hedge against exposure to variable cash flows of a probable forecasted transaction, it will record changes in the fair value of the derivative instrument in account 176, Derivative instrument assets-Hedges, or account 245, Derivative instrument liabilities-Hedges, as appropriate, with a corresponding amount in account 219.1, Other comprehensive income, for the effective portion of the hedge. The ineffective portion of the hedge transaction will be reflected in the same income or expense account that would have been used if the hedged item had been disposed of or settled. Amounts recorded in other comprehensive income will be reclassified into earnings in the same period or periods that the hedged forecasted item affects earnings.

3. In part 101, Balance Sheet Accounts, accounts 124, paragraph A, 125, 126, 127, 128, and 129 introductory text, are revised, and Accounts 175, 176, 219, 219.1, 244 and 245 are added to read as follows:

**Balance Sheet Accounts**

124 Other investments.
A. This account shall include the book cost of investments in securities issued or assumed by nonassociated companies, investment advances to such companies, and any investments not accounted for elsewhere. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments. Include also the offsetting entry to the recording of amortization of discount or premium on interest bearing investments. (See account 419, Interest and dividend income.)

125 Sinking funds (Major only).

This account shall include the amount of cash and book cost of investments held in sinking funds. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments. A separate account, with appropriate title, shall be kept for each sinking fund. Transfers from this account to special deposit accounts may be made as necessary for the purpose of paying matured sinking-fund obligations, or obligations called for redemption but not presented, or the interest thereon.

126 Depreciation fund (Major only).

This account shall include the amount of cash and book cost of investments which have been segregated in a special fund for the purpose of indentifying such assets with the accumulated provisions for depreciation. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments.

127 Amortization fund (Major only).
This account shall include the amount of cash and book cost of investments of any investments of any fund maintained pursuant to the requirements of a federal regulatory body, as the cash and investments segregated for the purpose of identifying the specific assets associated with account 215.1, Appropriated retained earnings Amortization reserve, Federal. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments.

128 **Other special funds (Major only).**

This account shall include the amount of cash and book cost of investments which have been segregated in special funds for insurance, employee pensions, savings, relief, hospital, and other purposes not provided for elsewhere. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments. A separate account with appropriate title, shall be kept for each fund.

* * * * * *

129 **Special funds (Nonmajor only).**

This account shall include the amount of cash and book cost of investments which have been segregated in special funds for bond retirements, property additions and replacements, insurance, employees’ pensions, savings, relief, hospital, and other purposes not provided for elsewhere. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments. A separate account, with appropriate title, shall be kept for each fund.

* * * * * *
175 **Derivative instrument assets.**

This account shall include the amounts paid for derivative instruments, and the change in the fair value of all derivative instrument assets not designated as cash flow or fair value hedges. Account 421, Miscellaneous nonoperating income, will be charged with the corresponding amount of the change in the fair value of the derivative instrument.

176 **Derivative instrument assets-Hedges.**

A. This account shall include the amounts paid for derivative instruments, and the change in the fair value of derivative instrument assets designated by the utility as cash flow or fair value hedges.

B. When a utility designates a derivative instrument asset as a cash flow hedge it will record the change in the fair value of the derivative instrument in this account with a concurrent charge to account 219.1, Other comprehensive income, with the effective portion of the derivative's gain or loss. The ineffective portion of the cash flow hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

C. When a utility designates a derivative instrument as a fair value hedge it will record the change in the fair of the derivative instrument in this account with a concurrent charge to a subaccount of the asset or liability that carries the item being hedged. The ineffective portion of the fair value hedge will be charged to the same income or expense
account that would have been used if the hedged item had been disposed of or otherwise settled.

* * * * *

219  Accumulated other comprehensive income.

A. This account shall include amounts of other comprehensive income transferred from account 219.1, Other comprehensive income. Records supporting the entries to this account shall be maintained so that the utility can furnish the amount of other comprehensive income for each item included in this account.

B. This account shall also be debited or credited, as appropriate, with amounts of accumulated other comprehensive income that have been included in the determination of net income during the period and in accumulated other comprehensive income in prior periods. Separate records for each category of items will be maintained to identify the amount of the reclassification adjustments from accumulated other comprehensive income to earnings made during the period.

219.1  Other comprehensive income.

A. This account shall include revenues, expenses, gains, and losses that are appropriately includable in other comprehensive income during the period. At year end the total of other comprehensive income will be transferred to account 219, Accumulated other comprehensive income.

B. This account shall also be debited or credited, as appropriate, with amounts of other comprehensive income that have been included in the determination of net income
in the same period. Separate records will be maintained to identify the amount of the reclassification adjustments to earnings during the period.

C. Examples of items of other comprehensive income include foreign currency items, minimum pension liability adjustments, unrealized gains and losses on certain investments in debt and equity securities, and cash flow hedges. Records supporting the entries to this account shall be maintained so that the utility can furnish the amount of other comprehensive income for each item included in this account.

* * * * * * * *

244 Derivative instrument liabilities.

This account shall include the change in the fair value of all derivative instrument liabilities not designated as cash flow or fair value hedges. Account 421, Miscellaneous nonoperating income, will be charged with the corresponding amount of the change in the fair value of the derivative instrument.

245 Derivative instrument liabilities-Hedges

A. This account shall include the change in the fair value of derivative instrument liabilities designated by the utility as cash flow or fair value hedges.

B. A utility will record the change in the fair value of a derivative instrument liability related to a cash flow hedge in this account, with a concurrent charge to account 219.1, Other comprehensive income, with the effective portion of the derivative’s gain or loss. The ineffective portion of the cash flow hedge will be charged to the same income
or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

C. A utility will record the change in the fair of a derivative instrument liability related to a fair value hedge in this account, with a concurrent charge to a subaccount of the asset or liability that carries the item being hedged. The ineffective portion of the fair value hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

* * * * *

PART 201-- UNIFORM SYSTEM OF ACCOUNTS PRESCRIBED FOR NATURAL GAS COMPANIES SUBJECT TO THE PROVISIONS OF THE NATURAL GAS ACT

4. The authority citation for part 201 continues to read as follows:


5. In part 201, General Instructions, 22. Accounting for other comprehensive income, and 23. Accounting for derivative instruments and hedging activities, are added to read as follows:

General Instructions

* * * * *

22 Accounting for other comprehensive income.

A. Utilities will record items of other comprehensive income in account 219.1, Other comprehensive income. Amounts included in this account will be classified by
their nature and supporting records will be maintained by each category of other comprehensive income. Examples of categories of other comprehensive income include, foreign currency items, minimum pension liability adjustments, unrealized gains and losses on available-for-sale type securities and cash flow hedge amounts.

B. At year end, amounts recorded in account 219.1, Other comprehensive income, will be transferred to account 219, Accumulated other comprehensive income. Supporting records will be maintained for account 219 so that the company can readily identify the cumulative amount of other comprehensive income for each item included in this account.

C. When an item of other comprehensive income enters into the determination of earnings in the current or subsequent periods a reclassification adjustment will be recorded in accounts 219 or 219.1 to avoid double counting of when an item included in net income was also included in other comprehensive income in the same or prior period.

23 Accounting for derivative instruments and hedging activities.

A. Utilities will recognize derivative instruments as either assets or liabilities in the financial statements and measure those instruments at fair value. A derivative instrument is a financial instrument or other contract with all three of the following characteristics:

1. It has one or more underlyings and a notional amount or payment provision. Those terms determine the amount of the settlement or settlements, and, in some cases, whether or not a settlement is required.
2. It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have similar response to changes in market factors.

3. Its terms require or permit net settlement, can readily be settled net by a means outside the contract, or provides for delivery of an asset that puts the recipient in a position not substantially different from net settlement.

B. The accounting for the changes in the fair value of derivative instruments depends upon their intended use and designation. Changes in the fair value of derivative instruments not designated as fair value or cash flow hedges will be recorded in account 175, Derivative instrument assets, or account 244, Derivative instrument liabilities, as appropriate, with the gains or losses charged to earnings in account 421, Miscellaneous nonoperating income.

C. A derivative instrument may be specifically designated as a fair value or cash flow hedge. A hedge may be used to manage risk to price, interest rates, or foreign currency transactions. Utilities will maintain documentation of the hedge relationship at the inception of the hedge that details the risk management objective and strategy for undertaking the hedge, the nature of the risk being hedged, and how hedge effectiveness will be determined.

D. If the utility designates the derivative instrument as a fair value hedge against exposure to changes in the fair value of a recognized asset, liability, or a firm commitment, it will record the change in fair value of the derivative instrument to account
176, Derivative instrument assets-Hedges, or account 245, Derivative instrument liabilities-Hedges, as appropriate, with a corresponding adjustment to the subaccount of the item being hedged. The ineffective portion of the hedge transaction will be reflected in the same income or expense account that would have been used if the hedged item had been disposed of or settled. In the case of a fair value hedge of a firm commitment a new asset or liability is created. As a result of the hedge relationship, the new asset or liability will become part of the carrying amount of the item being hedged.

E. If the utility designates the derivative instrument as a cash flow hedge against exposure to variable cash flows of a probable forecasted transaction, it will record changes in the fair value of the derivative instrument in account 176, Derivative instrument assets-Hedges, or account 245, Derivative instrument liabilities-Hedges, as appropriate, with a corresponding amount in Account 219.1, Other comprehensive income, for the effective portion of the hedge. The ineffective portion of the hedge transaction will be reflected in the same income or expense account that would have been used if the hedged item had been disposed of or settled. Amounts recorded in other comprehensive income will be reclassified into earnings in the same period or periods that the hedged forecasted item affects earnings.

* * * * * *

6. In part 201, Balance Sheet Accounts, Accounts 124, paragraph A, 125, 126, and 128, introductory test, are revised, and Accounts 175, 176, 219, 219.1, 244 and 245 are added to read as follows:
124 Other investments.

A. This account shall include the book cost of investments in securities issued or assumed by nonassociated companies, investment advances to such companies, and any investments not accounted for elsewhere. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments. Include also the offsetting entry to the recording of amortization of discount or premium on interest bearing investments. (See account 419, interest and dividend income.)

125 Sinking funds.

This account shall include the amount of cash and book cost of investments held in sinking funds. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments. A separate account, with appropriate title, shall be kept for each sinking fund. Transfers from this account to special deposit accounts may be made as necessary for the purpose of paying matured sinking-fund obligations, or obligations called for redemption but not presented, or the interest thereon.

126 Depreciation fund.
This account shall include the amount of cash and book cost of investments which have been segregated in a special fund for the purpose of indentifying such assets with the accumulated provisions for depreciation. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments.

128 Other special funds.

This account shall include the amount of cash and book cost of investments which have been segregated in special funds for insurance, employee pensions, savings, relief, hospital, and other purposes not provided for elsewhere. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments. A separate account with appropriate title, shall be kept for each fund.

175 Derivative instrument assets.

This account shall include the amounts paid for derivative instruments, and the change in the fair value of all derivative instrument assets not designated as cash flow or fair value hedges. Account 421, Miscellaneous nonoperating income, will be charged with the corresponding amount of the change in the fair value of the derivative instrument.

176 Derivative instrument assets-Hedges.
A. This account shall include the amounts paid for derivative instruments, and the change in the fair value of derivative instrument assets designated by the utility as cash flow or fair value hedges.

B. When a utility designates a derivative instrument asset as a cash flow hedge it will record the change in the fair value of the derivative instrument in this account with a concurrent charge to account 219.1, Other comprehensive income, with the effective portion of the derivative's gain or loss. The ineffective portion of the cash flow hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

C. When a utility designates a derivative instrument asset as a fair value hedge it will record the change in the fair of the derivative instrument in this account with a concurrent charge to a subaccount of the asset or liability that carries the item being hedged. The ineffective portion of the fair value hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

∗ ∗ ∗ ∗ ∗ ∗ ∗

219  Accumulated other comprehensive income.

A. This account shall include amounts of other comprehensive income transferred from account 219.1, Other comprehensive income. Records supporting the entries to this account shall be maintained so that the utility can furnish the amount of other comprehensive income for each item included in this account.
B. This account shall also be debited or credited, as appropriate, with amounts of accumulated other comprehensive income that have been included in the determination of net income during the period and in accumulated other comprehensive income in prior periods. Separate records for each category of items will be maintained to identify the amount of the reclassification adjustments from accumulated other comprehensive income to earnings made during the period.

219.1 Other comprehensive income.

A. This account shall include revenues, expenses, gains, and losses that are properly includable in other comprehensive income during the period. At year end the total of other comprehensive income will be transferred to account 219, Accumulated other comprehensive income.

B. This account shall also be debited or credited, as appropriate, with amounts of other comprehensive income that have been included in the determination of net income in the same period. Separate records will be maintained to identify the amount of the reclassification adjustments to earnings during the period.

C. Examples of items of other comprehensive income include foreign currency items, minimum pension liability adjustments, unrealized gains and losses on certain investments in debt and equity securities, and cash flow hedges. Records supporting the entries to this account shall be maintained so that the utility can furnish the amount of other comprehensive income for each item included in this account.
244 Derivative instrument liabilities.

This account shall include the change in the fair value of all derivative instrument liabilities not designated as cash flow or fair value hedges. Account 421, Miscellaneous nonoperating income, will be charged with the corresponding amount of the change in the fair value of the derivative instrument.

245 Derivative instrument liabilities-Hedges.

A. This account shall include the change in the fair value of derivative instrument liabilities designated by the utility as cash flow or fair value hedges.

B. A utility will record the change in the fair value of a derivative liability related to a cash flow hedge in this account, with a concurrent charge to account 219.1, Other comprehensive income, with the effective portion of the derivative's gain or loss. The ineffective portion of the cash flow hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

C. A will record the change in the fair of a derivative instrument liability related to a fair value hedge in this account, with a concurrent charge to a subaccount of the asset or liability that carries the item being hedged. The ineffective portion of the fair value hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

* * * * *
PART 352-- UNIFORM SYSTEMS OF ACCOUNTS PRESCRIBED FOR OIL PIPELINE COMPANIES SUBJECT TO THE PROVISIONS OF THE INTERSTATE COMMERCE ACT

7. The authority citation for part 352 continues to read as follows:


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8. In part 352 List of Instructions and Accounts, paragraph 35(d) is revised to read as follows:

Definitions.

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(d) "Cost," as applied to a marketable equity security, refers to the original cost as adjusted for unrealized holding gains and losses.

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9. In part 352, General Instructions, paragraph 1-15(a)(b) and (c) are revised, (d) and (e) are removed, and General Instructions paragraphs 1-17 and 1-18 are added to read as follows:

General Instructions

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1-15 Accounting for marketable securities owned. (a) Accounts 11 "Temporary investments," 20 "Investments in affiliated companies," and 21 "Other investments" shall be maintained in such a manner as to reflect the marketable equity portion (see definition 35) and other securities or investments.

(b) For the purpose of determining net ledger value, the marketable equity securities in account 11 shall be considered the current portfolio and the marketable equity securities in accounts 20 and 21 (combined) shall be considered the noncurrent portfolio.

(c) Carriers will categorize their security investments as held-to-maturity, trading, or available-for-sale. Unrealized holding gains and losses on trading type investment securities will be recorded in account 660, Miscellaneous income charges. Unrealized holding gains and losses on available-for-sale type investment securities will be recorded in account 77.1, Other comprehensive income.

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1-17 Accounting for other comprehensive income.

(a) Carriers will record items of other comprehensive income in account 77.1, Other comprehensive income. Amounts included in this account will be maintained by each category of other comprehensive income. Examples of categories of other comprehensive income include, foreign currency items, minimum pension liability adjustments, unrealized gains and losses on available-for-sale type securities and cash flow hedge amounts.
(b) At year end, amounts recorded in account 77.1, Other comprehensive income, will be transferred to account 77, Accumulated other comprehensive income. Supporting records will be maintained for account 77 so that the carrier can readily identify the cumulative amount of other comprehensive income for each item included in this account.

(c) When an item of other comprehensive income enters into the determination of earnings in the current or subsequent periods a reclassification adjustment will be recorded in accounts 77 or 77.1 to avoid double counting of when an item included in net income was also included in other comprehensive income in the same or prior period.

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1-18 Accounting for derivative instruments and hedging activities.

(a) A carrier will recognize derivative instruments as either assets or liabilities in the financial statements and measure those instruments at fair value. A derivative instrument is a financial instrument or other contract with all three of the following characteristics:

1. It has one or more underlyings and a notional amount or payment provision. Those terms determine the amount of the settlement or settlements, and, in some cases, whether or not a settlement is required.

2. It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have similar response to changes in market factors.
3. Its terms require or permit net settlement, can readily be settled net by a means outside the contract, or provides for delivery of an asset that puts the recipient in a position not substantially different from net settlement.

(b) The accounting for the changes in the fair value of derivative instruments depends upon their intended use and designation. Changes in the fair value of derivative instruments not designated as fair value or cash flow hedges will be recorded in account 46, Derivative instrument assets, or account 65, derivative instrument liabilities, as appropriate, with the gains or losses charged to earnings in account 660, Miscellaneous income charges.

(c) A derivative instrument may be specifically designated as a fair value or cash flow hedge. A hedge may be used to manage risk to price, interest rates, or foreign currency transactions. An entity will maintain documentation of the hedge relationship at the inception of the hedge that details the risk management objective and strategy for undertaking the hedge, the nature of the risk being hedged, and how hedge effectiveness will be determined.

(d) If the carrier designates the derivative instrument as a fair value hedge against exposure to changes in the fair value of a recognized asset, liability, or a firm commitment, it will record the change in fair value of the derivative instrument designated as a fair value hedge to account 47, Derivative instrument assets-Hedges, or account 66, Derivative instrument liabilities-Hedges, as appropriate, with a corresponding adjustment to the subaccount of the item being hedged. The ineffective portion of the
hedge transaction will be reflected in the same income or expense account that would have been used if the hedged item had been disposed of or settled. In the case of a fair value hedge of a firm commitment, a new asset or liability is created. As a result of the hedge relationship, the new asset or liability will become part of the carrying amount of the item being hedged.

(e) If the carrier designates the derivative instrument as a cash flow hedge against exposure to variable cash flows of a probable forecasted transaction it will record changes in the fair value of the derivative instrument in account 47, Derivative instrument assets-Hedges, or account 66, Derivative instrument liabilities-Hedges, as appropriate, with a corresponding amount in account 77.1, Other comprehensive income, for the effective portion of the hedge. The ineffective portion of the hedge transaction will be reflected in the same income or expense account that would have been used if the hedged item had been disposed of or settled. Amounts recorded in other comprehensive income will be reclassified into earnings in the same period or periods that the hedged forecasted item affects earnings.

10. In part 352, Balance Sheet Accounts, Accounts 11, 21, and 22 are revised, Accounts 23, 24, and 75.5 are removed, and Accounts 46, 47, 77 and 77.1 are added to read as follows:

**Balance Sheet Accounts**
11 Temporary investments.

(a) This account shall include the cost of securities and other collectible obligations acquired for the purpose of temporarily investing cash, such as United States Treasury certificates, marketable securities, time drafts receivable, demand loans, time deposits with banks and trust companies, and other similar investments of a temporary character. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments.

(b) This account shall be subdivided to reflect the marketable equity securities' portion and other temporary investments. (See Instruction 1-15).

21 Other investments.

This account shall include the cost of investments in securities of (other than securities held in special funds) and advances made to other than affiliated companies. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments. Separate records shall be maintained to show the securities pledged and the following classes of investments in each nonaffiliated company:

(a) Stocks.

(b) Bonds.

(c) Other secured obligations.

(d) Unsecured notes.
(e) Investment advances.

22 Sinking and other funds.

(a) This account shall include cash and cost of investments in securities and other assets, trusteeed or otherwise restricted, that have been segregated in distinct funds for purposes of redeeming outstanding obligations; purchasing or replacing assets; paying pensions, relief, hospitalization, and other similar items. This account shall also include unrealized holding gains and losses on trading and available-for-sale types of security investments. The cash value of life insurance policies on the lives of employees and officers to the extent that the carrier is the beneficiary of such policies shall also be included in this account. Separate subsidiary records shall be maintained for each distinct fund.

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46 Derivative instrument assets.

This account shall include the amounts paid for derivative instruments, and the change in the fair value of all derivative instrument assets not designated as cash flow or fair value hedges. Account 660, Miscellaneous income charges, will be charged with the corresponding amount of the change in the fair value of the derivative instrument.

47 Derivative instrument assets-Hedges.
(a) This account shall include the amounts paid for derivative instruments, and the change in the fair value of derivative instrument assets designated by the utility as cash flow or fair value hedges.

(b) When a carrier designates a derivative instrument asset as a cash flow hedge, it will record the change in the fair value of the derivative instrument in this account with a concurrent charge to account 77.1, Other comprehensive income, with the effective portion of the derivative's gain or loss. The ineffective portion of the cash flow hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

(c) When a carrier designates a derivative instrument as a fair value hedge, it will record the change in the fair of the derivative instrument in this account with a concurrent charge to a subaccount of the asset or liability that carries the item being hedged. The ineffective portion of the fair value hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

65 Derivative instrument liabilities.

This account shall include the change in the fair value of all derivative instrument liabilities not designated as cash flow or fair value hedges. Account 660, Miscellaneous income charges, will be charged with the corresponding amount of the change in the fair value of the derivative instrument.
66  Derivative instrument liabilities—Hedges.

(a) This account shall include the change in the fair value of derivative instrument liabilities designated by the carrier as cash flow or fair value hedges.

(b) A carrier will record the change in the fair value of a derivative instrument liability related to a cash flow hedge in this account, with a concurrent charge to account 77.1, Other comprehensive income, with the effective portion of the derivative’s gain or loss. The ineffective portion of the cash flow hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

(c) A carrier will record the change in the fair of a derivative instrument liability related to a fair value hedge in this account, with a concurrent charge to a subaccount of the asset or liability that carries the item being hedged. The ineffective portion of the fair value hedge will be charged to the same income or expense account that would have been used if the hedged item had been disposed of or otherwise settled.

77  Accumulated other comprehensive income.

(a) This account shall include amounts of other comprehensive income transferred from account 77.1, Other comprehensive income. Records supporting the entries to this account shall be maintained so that the utility can furnish the amount of other comprehensive income for each item included in this account.
(b) This account shall also be debited or credited, as appropriate, with amounts of accumulated other comprehensive income that have been included in the determination of net income during the period and in accumulated other comprehensive income in prior periods. Separate records for each category of items will be maintained to identify the amount of the reclassification adjustments from accumulated other comprehensive income to earnings made during the period.

77.1 Other comprehensive income.

(a) This account shall include revenues, expenses, gains, and losses that are properly includable in other comprehensive income during the period. At year end, the total of other comprehensive income will be transferred to account 77, Accumulated other comprehensive income.

(b) This account shall also be debited or credited, as appropriate, with amounts of other comprehensive income that have been included in the determination of net income in the same period. Separate records will be maintained to identify the amount of the reclassification adjustments to earnings during the period.

(c) Examples of items of other comprehensive income include foreign currency items, minimum pension liability adjustments, unrealized gains and losses on certain investments in debt and equity securities, and cash flow hedges. Records supporting the entries to this account shall be maintained so that the carrier can furnish the amount of other comprehensive income for each item included in this account.