Energy Regulatory Development in Bulgaria

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MANUAL TO THE REGULATORY CHART OF ACCOUNTS FOR THE PURPOSES OF REGULATORY ACCOUNTING OF DISTRICT HEATING COMPANIES

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Prepared by:

Pierce Atwood, LLP
48 Vitosha Blvd., 1000 Sofia, Bulgaria

Contact: Maya Hristova, Krassimir Kanev

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1. EXECUTIVE SUMMARY

The attached Manual to the Regulatory Chart of Accounts for the regulatory accounting purposes of the District Heating is part of a series of documents of Task III activities of the USAID/Bulgarian Energy Regulatory Development Project. The document provides the accounting and regulatory requirements for the licensees in the Bulgarian Electricity District Heating Companies, in accordance with the requirements of the Uniform Systems of Accounts for each sector (electricity, natural gas, and district heating), developed by the Pierce Atwood project earlier as part of Task III and adopted by the State Energy and Water Regulatory Commission (SEWRC).

The present manual is in full compliance with the regulatory accounting principles and requirements. Carriers of the regulatory accounting information are the Balance sheet and the Income Statement for the district heating companies ("DHCs") as well as the adopted additional regulatory reporting forms. Information in these reporting documents is classified and structured in such a way that it would allow for the regulatory body to monitor and control the respective legal parameters and requirements.

The uniform Chart of Accounts for regulatory accounting of DHCs should comply to a great extent with the National Chart of Accounts and the Accountancy Act, with utility practice and with the international financial reporting standards applied by these utilities. The objective is for the new regulatory framework requirements for regulatory accounting and reporting to be fulfilled in a most expedient way so that efforts for restructuring information by the licensed entities are minimized.

The uniform Chart of Accounts covers all sections of the National Chart of Accounts. Selection of groups conforms to the nature of the licensed activity. The majority of content nature, item numbers, and section, group and account descriptions are preserved while new account specifications are added according to the new requisites.

It is recommended to add accounts with three, four and five digit codes in addition to the analytics. The detailed specifications of accounts carrying the information that have greater importance for the regulatory body purposes have been proposed.

The content of this recommended methodology to be used with the Uniform Chart of Accounts includes:

- Balance sheet sections and items and financial accounts as per the Uniform Chart of Accounts being carriers of the standardized information for the purposes of regulatory accounting; and,

- Sections and items in the Income Statement and the respective accounts as per the Unified Chart of Accounts being carriers of the standardized information for the purposes of regulatory accounting.

2. DEFINING REGULATED ACTIVITIES AND THEIR INTERNAL STRUCTURE

The activities that are regulated by the regulatory body are: production of electricity, production, transmission and supply of thermal energy and connecting of consumers.

District Heating Company

REGULATED ACTIVITY		**NON-REGULATED ACTIVITY**
1.Production of electricity		
2a.Production **2b.Transmission and** **2c.Supply of thermal energy**		
3. Connection of consumers		

The major aspects of the activities of production of electricity, production, transmission and supply of thermal energy and connecting of consumers that are a subject to monitoring are:

- Revenue from the main activity, including:
  - Income from electricity sales
  - Income from Sales of thermal energy by consumer groups
- Revenue from connections
- Expenses for the main /core/ activity, including:
  - Fuel expenses
  - Operation expenses
  - Repair expenses
- Expenses for Non-Core Operations, including:
  - Fuel expenses
  - Service stations and work shop expenses
  - Repair shop expenses
  - Laboratories and research centers expenses
  - Expenses for other Non-Core Operations
- Research and development expenses

- General and administrative expenses
- Capital construction expenses
- Connection of consumers expenses

3. CLASSIFICATION AND STRUCTURE OF REVENUES

In accordance with IAS 18 requirements, the income from the company's activities are reported as revenue, received from the following types of transactions and operations:

1. Sales of production;
2. Sales of goods;
3. Rendering of services; and,
4. Leasing out company's assets to third parties, against certain interest, obtaining revenues from rights and dividends.

Services could be provided over a certain period or over more than one period. Some contracts for rendering services shall be directly related to construcion contracts, for example, designer's services. Revenues from these contracts shall be considered in compliance with the construction contracts' requirements.

Revenue is the gross inflow of economic benefits during the period arising from the ordinary operating activities of a utility where this inflow results in increase of utility net worth other than increases related to shareholder's contributions.

Revenues include only gross inflow of economic benefits, while amounts collected by third parties like sales tax, commodity and service taxes, value added tax, etc. are not considered economic benefits received by utility and do not result in net worth increase. Therefore they are not part of the revenues.

Commodity sales revenue shall be recognized when the buyer takes on him/her considerable risks and benefits from ownership over commodity.

Revenue from rendering services shall be recognized on the basis of the phase of completion of the related service, determined as a percent ratio of services rendered at the time and the complete amount of services that is expected to be performed..

Revenues from interest bearing accounts shall be recognized on time proportion principle in relation to the remaining period of time and the effective interest for the maturity period, in cases where it has been determined that such a revenue will be accrued to the utility.

3.1. IDENTIFYING REVENUES BY REGULATED ACTIVITY FOR THE REGULATORY ACCOUNTING PURPOSES

For the purpose of the regulatory mechanism the identification of income by activity mechanism has been adopted:

1. Income from electricity production;
2. Income from heat production;
3. Income from transmission and supply of heat services
4. Income from connections;
5. Income from non-regulated activity.

Each of these activities has specific characteristics that allow for it to be distinguished accounting-wise. This separation of revenue accounting also allows for monitoring, metering and control through the accounting mechanisms for the purposes of the Regulator. At the same time, the consolidation of the regulated activities allows for a comprehensive management of the process in compliance with the National Energy Policy.

In order to unbundle the licensed activities, the DHCs need to do the following:

1. To identify and separately account the revenues from non-regulated activities;
2. To specify the revenues by types of regulated activity and by consumer groups.

The accounts for revenues by activities are put together in sub-group 71 – "Expenses for the activity" of group 7.

For the purposes of regulatory mechanism, each account of the revenues category that has direct or indirect relevence to the regulated characteristics of the DHCs shall be added with subaccounts to allow enough detail for monitoring and control purposes.

Accounts in group 70 are organized by the following types of transactions and events:

1. Income from Sales of Production;
2. Income from Sales of Merchandise;
3. Income from Sales of System Services; and,
4. Income from usage of utility assets by other persons, which shall bring about interests, dividends and royalties.

Account 711 stands for income from sales of production. The account has the following sub-accounts:

- Income from sales of electricity;
- Income from sales of thermal energy; and,
- Income from sales of production from non-regulated activities

Account 713 stands for income from rendering of services. The account has the following sub-accounts:

- Income from transmission and supply of thermal energy;
- Income from connection of consumers; and,
- Income from rendering of non-regulated services,

Accounts 711 and 713 have sub-accounts that reflect the consumer groups.

4. CLASSIFICATION AND STRUCTURE OF OPERATING EXPENSES

The structure of the chart of accounts is prepared in detail for the purposes of regulatory accounting and where necessary it would allow retrieval of additional information beyond the reporting classification included in the Income Statement of DHCs for the purposes of regulatory accounting.

Apart from statements related to cash flows, utilities shall prepare their financial statements using the principle of accruals.

In accounting, based on the principle of accruals, operations and events are recognized in the time of their occurrence, and not in the time of cash or cash equivalents receipt or payment;

and these events and operations shall be posted in accounting registers and reported in the financial statements for the period in which they occurred..

Expenses are recognized in the Income Statement in direct connection of expense incurrence with income from direct revenue carriers (matching). However the principle (concept) of matching does not make it possible to recognize balance sheet items, which do not meet the definition of asset or liability - costs shall not be recognized as assets in case that they cannot be matched with specific revenue in the following accounting periods. Revenues shall not be recognized as liabilities in case that they cannot be matched with specific cost in the following accounting periods.

Calculation accounts of group 60 are intended for reporting expenses by economic elements , and calculation accounts of group 61 are intended for reporting operating expenses.

IDENTIFYING EXPENSES BY REGULATED ACTIVITY FOR REGULATORY ACCOUNTING PURPOSES

For the purpose of the regulatory mechanism the identifying of expenses by activity mechanism has been adopted:

1. Expenses for electricity production;
2. Expenses for heat production;
3. Expenses for transmission of heat services
4. Expenses for heat supply services
5. Expenses for connections; and,
6. Expenses for non-regulated activity.

Each of these activities has specific characteristics that allow for it to be distinguished accounting-wise. It also allows for monitoring, metering and control through the accounting mechanisms for the purposes of the Regulator. At the same time, the consolidation of the regulated activities allows for a comprehensive management of the process in compliance with the National Energy Policy.

In order to unbundle the licensed activities, the DHCs need to do the following:

1. To identify and separately account for the expenses for non-regulated activities;
2. To specify and allocate the direct costs by types of regulated activity and by consumer groups. (In determining the value of electricity and heat they might use calculation schemes by activities and energy sites.);
3. To identify indirect production costs and propose a well justified mechanism for their allocation; and,
4. To identify costs for each regulated activity along the production chain in order to construct their internal structure.

Identifying expenses by economic elements

The accounts for expenses by economic elements are to be found in sub-group 60, “Expenses by economic elements,” of group 6.

The accounts are operational and are kept with net turnovers, in order to provide data for filling the Income Statement. Changes in the initially recorded amounts (returned materials non-utilized in the production, incorrectly accrued remunerations, etc.) shall be made only through deductible entries..

The accounts of group 60 are organized by economic elements:

601 Materials

602 Hired services

603 Depreciation costs

604 Wages

605 Social Security and allowances

606 Other Expenses

The analytical accounting of the group 60 accounts is organized according to the information needs for monitoring purposes by monitored objects/sites.

- Fuel expenses
- Operating expenses
- Repair expenses
- Expenses for supporting activities
- Research and development expenses
- Capital construction expenses
- Expenses related to connections of consumers;
- Administrative and General Expenses
- Expenses for non-regulated activity

At the end of the reporting period, the accounts in group 60 shall be closed down (credited against debiting) of the accounts of group 61. Operating expenses and group 207 Expenses for acquisition of fixed tangible assets.

Accounts 601 Expenses for materials, 602 Expenses for hired services, 603 Depreciation costs, 604 Expenses for Wages, 605 Social Security and allowances correspond completely to the accounts with the same numbers from the National Chart of Accounts (Council of Ministers Degree № 65 1998). It is important to state that expenses for materials, hired services, depreciation, wages and social security before being referred to the accounts in group 60 should be classified by functions for their further allocation to the accounts in group 61.- Operating expenses. This could be achieved in two ways: a) by adding analytical levels to the group 60 accounts; or b) by referring the respective expenses simultaneously (reflected in the analyzed initial document) to the account credit in group 60 and to the respective account debit in group 61. We recommend the second option in order to simplify the analytical accounting system.

All expenses for the activity that are not referred to other accounts in group 60 are to be reported in account 606. The account is concluded by the respective accounts in group 61.

Identifying expenses by activities

The accounts for expenses for the activities are to be found in sub-group 61, “Expenses for the activities,” of group 6.

Each of the expense articles shall be further detailed to the level subject to monitoring and control by the regulatory authority and having either direct or indirect relation to the regulated characteristics of the DHCs.

The major operation expenses (direct production expenses) are reported in account 611.

Account 611 is broken down further in accordance with the main licensed activities:

- Expenses for Electric Power Production
- Expenses for Thermal Power Production
- Expenses for thermal power transmission

The specificity of the operations of the DHCs presupposes the existence of certain expenses that are common for the two licensed activities - Electric Power Production and Thermal Power Production. These common production costs shall be allocated to the operations on rational and consistent basis. The allocation is based on the respective operational analysis and calculations.

The other two groups of production expenses (indirect production costs) that are subject to allocation are the expenses for non-core operations and the general administrative-management expenses. These expenses shall be reported in accounts 612 and 617. These accounts are further broken down by the main licensed activities with the aim of further allocating the non-core operations expenses and repair expenses to the main licensed activities (by closing down the sub-accounts of this account to the sub-accounts of account 611). Also for the purpose of monitoring:

- Account 612 is further broken down for the types of non-core activities; and,
- Account 617 is further broken down for the types of repairs.

Instead of further break down of these accounts for the purpose of analyzing them, the debit turnovers of the accounts for the licensed activities could be used with the respective sub-accounts of the accounts in group 60.

Account 615 shall reflect the costs for goods sold. It is further broken down into:

- Expenses for selling of electricity; and,
- Expenses for selling of thermal power.

Account 614 shall reflect all expenses related to general administrative organization of the production process and shall be broken down by types of expenses.

General administrative-managerial expenses are allocated between the regulated and non-regulated activities. The basis for this allocation is the relative share of revenues generated by the respective activities to the overall income from operations of the DHC.

Administrative-managerial expenses for regulated activities could be allocated to the main licensed activities/operations.

It is essential to state that direct and indirect operational expenses by their features - can be grouped into:

- Relatively constant costs
- Variable costs

For example, depreciation costs and building and plant maintenance espenses are relatively constant costs. Variable general costs cover auxiliary materials expenses, expenses for remuneration of personnel hired for general production activities, etc.

5. CLASSIFICATION AND STRUCTURE OF ASSETS

An asset is classified as current asset when:

1. It is expected that the asset shall be sold or it will be held with the purpose to be sold or used during the normal operating cycle of utility or;
2. It is held mostly for a commercial purpose or for a short period of time and it is expected to be sold within 12 months of the balance sheet date; or
3. It represents cash or cash equivalents with no restrictions on its spending.

All other assets are classified as non-current/fixed.

Current assets comprise inventory and trade receivables, which are sold, used or brought into effect during the normal operating cycle of utility, even if it is not expected for them to be brought into effect within the following 12 months after the balance sheet date. Trading securities are defined as current assets if it is expected for them to be brought into effect within the following 12 months after the balance sheet date; otherwise they are defined as non-current assets.

5.1. CLASSIFICATION AND STRUCTURE OF TANGIBLE FIXED ASSETS.

This document has been prepared in accordance with IFRS 16, Property, plant and equipment and also it has been put in detail for the purposes of regulatory accounting.

The usual accounts of Section 2 - Fixed asset accounts, group 20, Tangible fixed assets, shall be used to report tangible fixed assets for the purposes of regulatory accounting. They would typically include:

201	Land
202	Not used
203	Buildings
204	Machinery, plant and equipment
205	Vehicles
206	Implements
207	Expenses for acquiring fixed assets
208	Fixed Tangible assets taken out of operation
209	Other tangible fixed assets

These accounts are detailed by several characteristics of the elements of one sub-class of assets taking into consideration their characteristics. This is only possible because the elements of one of the sub-classes belong to a certain class: The characteristics include: a) type of activity: core, non-core, administration and management etc.; b) type of licensed activity: production of energy (electricity-, heat-, and general), transmission of thermal energy, non-regulated activities etc. c) asset class (the life of assets is taken into consideration): metering devices and equipment, computers and communication systems etc.

5.1.1. Classification and structure of intangible fixed assets

The accounts for reporting- Intangible fixed asset accounts constitute group 30, “Materials, production and goods” of group 3.

Account 302 “Materials” is further detailed by groups of materials as follows:

- Fuels for technological needs
- Other fuels
- Oils
- Technological water
- Chemicals
- Spare parts
- Merchandise - pipes, cables etc.
- Stationery and other materials used for administration and management
- Other materials

Sub-accounts of 302 are further detailed depending on the types of materials.

5.1.2. Classification and structure of receivables

Account 411 “Customers” are to be detailed by types of receivables from sales (including all types of regulated and non-regulated activities) for all customer groups.

6. CLASSIFICATION AND STRUCTURE OF LIABILITIES

For the purposes of regulatory mechanism accounts liabilities shall be classified taking into consideration the following requirements:

1. Sub-accounts of account 12 «Financial results (Profit or Loss)» are detailed by the results from the regulated and non-regulated activity; and,
2. Sub-accounts of account 401 « Suppliers» are detailed on the basis of liabilities to suppliers for the regulated and non-regulated activity.