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Nancy M. Morris
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100 F Street, N.E.
Washington, DC 20549-1090

Submitted via e-mail to rule-comments@sec.gov

Re: File Number 265-24

The Edison Electric Institute respectfully submits these comments in response to the *Progress Report of the SEC Advisory Committee on Improvements to Financial Reporting* (Progress Report) that the Securities and Exchange Commission (SEC or the Commission) published at 73 Fed. Reg. 10898 on February 28, 2008.

The Edison Electric Institute (EEI) is the association of U.S. shareholder-owned electric companies. Our members serve 95 percent of the ultimate customers in the shareholder-owned segment of the industry, and represent approximately 70 percent of the U.S. electric power industry.

First, we applaud the Commission's efforts to form this Committee and work toward a more consistent and practical framework to improve financial reporting. We would anticipate many benefits emanating from the recommendations as we move toward global convergence. Specifically, as financial statement preparers, we view the proposed recommendations on materiality, error correction and a framework for accounting judgments to be critical steps in achieving the overall goal of reduced complexity and more principles based accounting standards. These recommendations will have a direct positive impact on one of the most significant causes of financial reporting complexity – the fear of "second guessing" and the risk of litigation.

One of the Advisory Committee's recommendations was that:

> "GAAP should be based on business activities rather than industries. As such, the SEC should recommend that any new projects undertaken jointly or separately by the FASB be scoped on the basis of business activities rather than industries. Any new projects should include the elimination of existing industry-specific guidance in relevant areas as a specific objective of those projects, unless, in rare circumstances, retaining industry guidance can be justified on the basis of cost-benefit considerations (discussed in section II.A of Chapter 1).
>
> The SEC should also recommend that, in conjunction with its current codification project, the FASB add a project to its agenda to remove or minimize existing industry-specific guidance that conflicts with generalized GAAP, taking into account the pace of convergence efforts. (Chapter 1 – developed proposal 1.1)."

As detailed in Appendix B of the Progress Report, the Industry-Specific Guidance referred to by the Committee includes Financial Accounting Standards Board (FASB) Statement No. 71, *"Accounting for the Effects of Certain Types of Regulation"* (SFAS 71).

EEI believes that SFAS 71 does not represent "industry-specific guidance" as contemplated by the Advisory Committee, and accordingly, should not be eliminated. Rather, SFAS 71 articulates the appropriate accounting for the economic effects of the actions of regulatory bodies. The guidance in SFAS 71 can be followed by any enterprise with rate-regulated operations that meet its three specific criteria. A company which is considered or called a public utility cannot automatically apply SFAS 71 in its general-purpose external financial statements – only a company which has a business activity meeting the three SFAS 71 criteria can apply the accounting standard to that portion of its business. These business activities cross a variety of industries that have different economic drivers, risks, performance metrics, investors, and other stakeholders, including electric generation companies, electric transmission and distribution companies, gas distribution companies, and water companies. Thus, we believe this standard clearly applies to certain "business activities" versus a single industry as a whole, and its provisions are focused on fairly presenting the economic effects on existing assets and liabilities resulting from past transactions as the result of actions of regulatory bodies. Accordingly, this standard is essential in that it provides clear guidance to assure consistent presentation of the results of these business activities across industries and should be retained.

SFAS 71 is not different in concept from SFAS 109, which governs the accounting for the effects of taxes imposed by taxing authorities, as illustrated below:

- Rate regulators determine the amount and timing of revenue an enterprise can collect; taxing authorities determine the amount and timing of taxes that an enterprise must pay.
- SFAS 71 provides guidance on accounting for the effects of rate regulation on assets and liabilities resulting from past transactions; SFAS 109 provides guidance on accounting for assets and liabilities resulting from the tax effects of past transactions.
- Actions of rate regulators result in regulatory assets and liabilities, representing probable future cash inflows or outflows as a result of the rate setting process; actions of taxing authorities result in deferred income tax assets and liabilities, representing probable future cash inflows or outflows as a result of the tax collection process.

Thus, SFAS 71 provides clear and necessary guidance for the economic effects of the rate setting activities of external, government-related bodies, just as SFAS 109 provides similar guidance for the economic effects of tax setting activities of similar external, government-related bodies.

Discussion of "Regulatory" Assets and Liabilities

A key aspect of SFAS 71 is the recording of regulatory assets and liabilities that reflect the economic effect on business activities as a result of the underlying rate making processes.

"Regulatory" Asset

A regulator has the ability to allow an entity with rate-regulated operations to recover prudently incurred expenditures through future rates charged to customers. Once such amounts have been approved by the regulator, the entity will recover the amounts in rates over a specified period. Under these circumstances, the entity would look to existing standards and the Conceptual Framework to determine whether an asset exists.

The asset represents an entity's right to increase future rates from what they would otherwise receive due to past events (i.e., the incurring of costs related to the past delivery of the regulated service that the entity has not yet had an opportunity to recover through rates). The higher rates will produce economic

benefits for the entity in the form of higher revenues and increased cash flows. To the extent that a regulated entity will be allowed to increase future rates from what they would otherwise be, it will be able to control the resulting benefits produced by that asset – i.e., it will be able to charge and collect the resulting revenues.

"Regulatory" Liability

A regulator may also impose an obligation on an entity with rate-regulated operations to return to its customers through future rate reductions amounts that it has collected in a current or prior period. Once rate reductions have been approved by the regulator, the entity will return the amounts to customers through reduced rates over a specified period. Under these circumstances, the entity would record a liability that reflects an entity's present obligation to reduce future rates from what they would otherwise receive due to past events. The lower rates will produce an outflow of economic benefits for the entity in the form of lower revenues and cash flows. Additionally, a regulator may provide for amounts to be collected in current rates to be used to cover costs expected to be incurred in the future (or, if not used for that purpose, to be returned to the customer by a reduction in future rates). The rate-regulated entity remains accountable to its customers, creating an obligation either to fund future specific expenditures without additional future rate relief (i.e., resulting in lower future rates than would otherwise be expected if the rate increase were timed to coincide with the cash expenditure) or to return those funds to the customer. The amounts collected in current rates are appropriately recorded as an obligation of the entity until used for the intended purpose or refunded to customers.

Users of Financial Statements

EEI believes that the accounting presented by SFAS 71 meets the needs of users of rate-regulated entities' financial statements and is a relevant consideration in evaluating the Committee's recommendation. Financial statements that include audited regulatory asset and liability balances reflecting the economic effects of rate regulation are essential for investors to understand the effects of that regulation on the entities business activities. Because the actions of regulators have an economic effect that directly impacts the entity's future cash flows and has what is essentially the force of law by which collectibility is affirmed, it is appropriate and useful to readers of the GAAP financial statements that those effects be recognized in the financial statements.

Summary

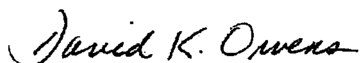
In summary, a regulator can change the future revenue streams of an enterprise subject to its jurisdiction as a result of past transactions or events. Economic benefits result from higher rates that will be collected by the rate-regulated entity, leading to increased revenues and cash flows, thus representing a GAAP asset in periods prior to collection. Alternatively, economic obligations result from reduced rates that will be collected in the future from customers, leading to reduced revenues and cash flows, thus representing a GAAP liability in periods prior to the use or refund of those amounts. As this illustrates, a regulator's actions clearly have a direct economic impact on an entity with rate-regulated operations, and we believe that this impact should be recognized in the entity's GAAP financial statements. SFAS 71 provides the accounting guidance for such recognition and results in reporting that is consistent with the actual economics of the regulatory process, something that would not result in the absence of this important accounting standard. The resulting financial reporting more accurately portrays the economic effect of the regulatory process that is desired by investors and other users of the financial statements of entities with these types of business activities.

In conclusion:

- SFAS 71 does not represent "industry-specific" guidance since it governs the accounting for the economic effects of the underlying business activities – specifically the unique aspects of cost-based rate regulation - and is applied by different companies across various industries.
- Elimination of SFAS 71 would result in financial statements that are less representative of the underlying business activities and economics that exist in a cost-based, rate regulated environment.

We appreciate the Commission's consideration of these matters and welcome the opportunity to discuss any and all related matters.

Sincerely,



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