March 13, 2012

Technical Director
Financial Accounting Standards Board
401 Merit 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: Exposure Draft – Revenue Recognition (Topic 605)
File Reference No. 2011-230

Edison International (Edison) appreciates the opportunity to provide comments on the FASB's Proposed Accounting Standards Update on Revenue Recognition (Topic 605) (the ED). Edison is the parent company of Southern California Edison (SCE), one of the nation’s largest electric utilities, and Edison Mission Group, a competitive power business.

We support the FASB’s efforts to improve the quality of financial statements and establishment of a revenue standard that applies across all industries. We fully support the core principle in the ED that “an entity shall recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services.” Our comments included below relate to accounting for power purchase agreements and the disclosure guidance set forth in the ED. We also participated in the preparation of the comment letter submitted by the Edison Electric Institute and support the contents set forth therein.

Accounting for Power Purchase Agreements (PPA)

Accounting for PPAs has been a topic of deliberations over the years due to their complexity. Under current accounting guidance, we evaluate a PPA to determine whether there is a variable interest in a variable interest entity, a derivative, or whether a PPA contains a lease. In the event that a PPA is not covered by the accounting literature in these areas, we recognize revenue on the accrual basis which generally means as electricity is delivered. The amount of revenue recognized is generally based on the quantity delivered times the contract price set forth in the PPA. The vast majority of PPAs are unit prices (which may be variable or fixed) or prices intended to compensate the seller for fixed costs (e.g. payments to ensure the availability of a generation resource), or a combination of the two.

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We refer to power purchase agreements in this letter or PPAs as the common term used in our industry. Such agreements are for the sale of electricity either from a generation source (e.g. wind or natural gas plants) or on a wholesale basis to commercial and industrial end use customers and may include additional products and services.

Including PPAs covered under EITF 91-6, Revenue Recognition of Long-Term Power Sales Contracts and EITF 96-17 - Revenue Recognition under Long-Term Power Sales Contracts That Contain both Fixed and Variable Pricing Terms.
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For PPAs that are accounted on the accrual basis under current generally accepted accounting principles in the United States (U.S. GAAP), the recognition of revenue by a seller is the same accounting as the purchaser. Since our subsidiaries are active in the sale and purchase of electricity, the consistency of the accounting models for both sides of the same transaction type provides objective, understandable and useful information for investors. With regards to revenue recognition from electricity sales pursuant to PPAs, we agree with the guidance set forth in paragraph 70 that “an entity shall allocate the transaction price to each separate performance obligation in an amount that depicts the amount of consideration to which the entity expects to be entitled in exchange for satisfying each separate performance obligation.” We believe that this guidance reflects the core principle set forth by the Board and that recognizing PPA revenue based upon quantities of electricity delivered multiplied by the contractual price is consistent with this guidance.

Some have raised questions that application of the provisions of the ED could result in a different pattern of revenue recognition. Consider the following example:

An electricity generator (“generator”) submits a bid in response to a utility’s request for offer (“RFO”) for 100 megawatts of new renewable electricity generation. Under the terms of the RFO, the generator is required to sell all of the output of the facility to the utility at a fixed unit price from the designated facilities for a period of twenty years. The generator is not permitted to sell the output to any other party. The generator is required to maintain the facility using prudent industry standards and to deliver a minimum number of megawatt hours of electricity.

The generator offers a fixed unit price for each megawatt hour of electricity to be generated and sold from the facility. The fixed unit price is designed to recover the capital costs of the project, operations and maintenance and other operating expenses, financing costs and provide for a reasonable a return on the generator’s investment.

The generator is awarded the PPA, constructs the renewable generation resource and begins to sell power to the utility.

Assuming the above example is accounted for on an accrual basis\(^3\), the generator would recognize revenue each period under current U.S. GAAP based on the megawatt hours delivered times the fixed unit price.

Alternative Interpretations of the ED:

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**Interpretation A:**

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\(^3\) This example assumes that the PPA is not a lease under new guidance for lease accounting that would be effective at the same time as the ED on revenue recognition.
Each megawatt hour of electricity sold under the PPA is distinct under paragraph 28, as the customer can benefit from each megawatt hour on its own. Under paragraph 50, the generator determines the transaction price as the expected megawatt hours of electricity to be generated over the term of the contract times the fixed unit price. The generator then follows paragraph 70 and allocates the transaction price to each megawatt hour using the guidance set forth in paragraph 73 (observable prices are not available in the marketplace for each megawatt hour for the term of the contract). Based on guidance in paragraph 72, the generator interprets the ED as indicating that use of market information is preferable to unit prices set forth in a contract. Accordingly, the generator develops a forward price curve for the contract term comprised of two components: (1) observable market prices from broker quotes in liquid markets (with variability for time of day and seasonal differences) and, then, adjusts for location differences between liquid markets and point of delivery, and (2) develops internal financial models for all remaining periods extrapolated for time of day and seasonal differences. Based on this company-specific forward curve, the generator allocates the transaction price to projected individual performance obligations.

Interpretation B:

Each megawatt hour of electricity sold under the PPA is distinct under paragraph 28, as the customer can benefit from each megawatt hour delivered on its own. Under paragraph 50, the generator views each fixed unit price as the transaction price for each distinct performance obligation. The generator considers suitable estimation methods described in paragraph 73 and guidance set forth in paragraph 42:

“If an entity has a right to invoice a customer in an amount that corresponds directly with the value to the customer of the entity’s performance completed to date (for example, a service contract in which an entity bills a fixed amount per hour of service provided), the entity shall recognize revenue in the amount to which the entity has the right to invoice.”

The generator concludes that the fixed unit price in the contract represents the amount of consideration expected to be entitled in exchange for satisfying each separate performance obligation and, accordingly, establishes a method of accounting that is consistently applied for similar facts and circumstances.

We believe that revenue recognition as described in Interpretation B represents the economics of the transaction and provides the most useful information to investors. Furthermore, Interpretation B better reflects accounting for groups of transactions when hedges, for example, are entered into to mitigate the risks of a PPA or an entity enters into contracts to purchase power as a means to meet the supply obligations under a PPA. In both of these cases, the gross margins reported under Interpretation B better reflect the commercial objectives of an enterprise and presented useful to investors. We believe that Interpretation A would not be appropriate for a number of reasons, including use of subjective information that would reduce the reliability and usefulness of financial statements for investors.

In order to reduce the potential for diversity in practice for similar contracts, we recommend revisions to:
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- Paragraph 50 to provide for the use of separate transaction prices for distinct performance obligations when such information is available from arm’s length transactions entered into at market prices.
- Paragraph 73 to provide for the use of output methods (as described in paragraph 42) as a suitable estimation method when the functional use of a product or service is the same for all separate performance obligations.

We also suggest that clarification be provided that paragraph 30 can be applied to the same homogenous product delivered over time. In the above example, we believe revenue recognition should be the same whether or not multiple performance obligations are satisfied at points in time or a single performance obligation is delivered over time.

Disclosure

We believe that the disclosure requirements of the ED are intended to provide information to investors for performance obligations under contracts with customers for future periods (whether at points in time in the future or a single performance obligation delivered over time). We do not believe that the disclosure requirements should be applied to contracts with customers for point of sale transactions. For example, Southern California Edison delivers electricity to customers under tariffs where usage is determined by the customer. Although we understand that these activities are within the scope of the ED, we do not believe that disclosure set forth in paragraph 117 is meaningful to investors nor cost beneficial to prepare. Accordingly, we suggest the final standard clarify that paragraph 117 does not apply to point of sale transactions similar to the practical expedient provisions of paragraph 121.

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We appreciate the opportunity to provide our views and suggestions. We are available to discuss the foregoing comments at your convenience.

Sincerely,

Mark C. Clarke  
Vice President, Controller