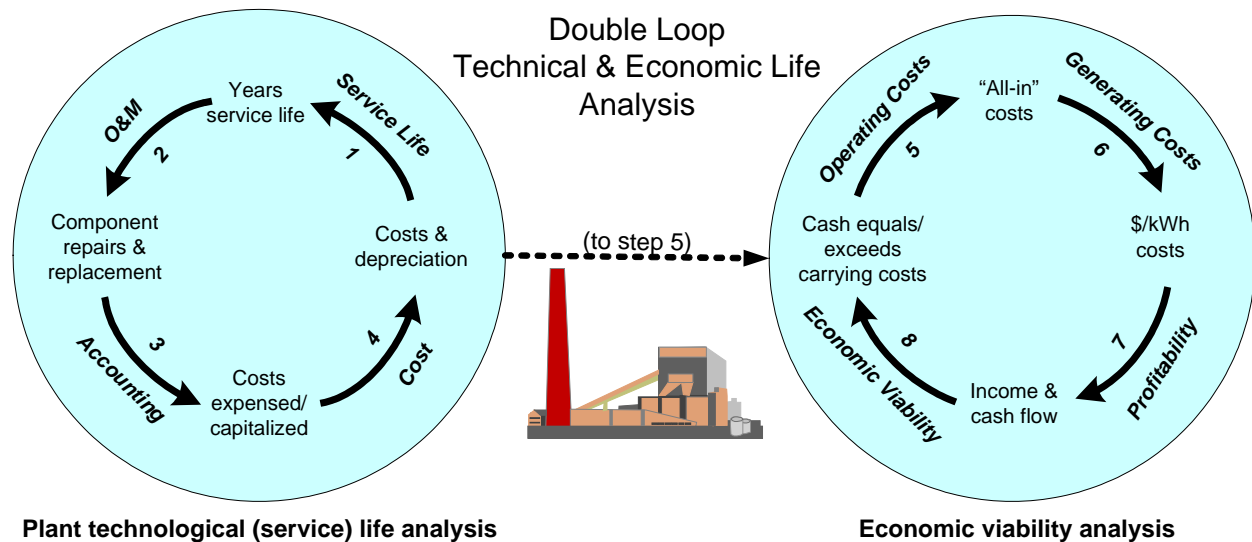


Power Magazine Article¹

Transactive Management has completed an 18-month study for the PG&E National Energy Group (NEG) that recommends using a depreciable life of over 45 years for fossil-fired plants and up to 100 years for its hydroelectric generating systems.

Depreciable life was determined by estimating the service life of components in a system-by-system breakdown of original plant construction cost. This considered how repairing, replacing and upgrading original components extends service life as well as the accounting treatment of costs incurred.

By including service life and maintenance cost estimates in cash flow projections, economic viability was validated by showing that capitalized costs could be fully recovered consistent with accounting requirements for testing asset impairment. The figure below depicts the steps completed in conducting a “double loop” analysis.



The study also found that plants that are regularly cycled should use a unit of production method to adjust service life projections. It recommends a production-based maintenance approach to identify hours and starts based operational factors to measure this impact on a component-level basis.

Recognizing depreciable life can have a significant effect on book value and income. For example, if a company with 10 GW generating capacity increases average depreciable life from 35-to-45 years, this could add over \$20 million a year to book income.

Ray Mischkot, President of Transactive Management, who conducted the study points out that; “this does not increase cash but does increase corporate earnings per share, which, in turn, influences the valuation and transaction price of publicly traded stock. This means that the governance and accounting provisions of the Sarbanes-Oxley Act may apply. The study, therefore, included recommendations for on-going company monitoring of the plant, company, industry and broader business climate factors upon which depreciable life conclusions were based.”

From:
Ray Mischkot
July 24, 2003

¹ This write-up was submitted to Power Magazine and appeared in the September 2003 issue at pages 14 and 15 of the Global Monitor section under the heading “New study on valuing plants”. The wording was somewhat modified by the editors for this version.