Regulated Utility Annual Revenue Requirements (RR)

- RR = (V – D) x (r) +E + d where
  - RR = annual revenue requirement
  - V = valuation of the assets devoted to utility service
  - D = accumulated depreciation, reduces valuation by the sum of each year's depreciation since an asset was put to utility service.
  - V – D net assets in service
  - r = rate of return (weighted average of the cost of debt and equity)
  - E = annual expenses
  - d = annual depreciation (Σ d = D)

RR = (V – D) x (r) +E + d

- Traditionally RR is a one-time calculation that occurs when the utility comes in for a rate proceeding occurring over a period of several years.
- Valuation (V) requires that the assets be “used and useful”. Assets that are not used and useful are excluded from V. Most utility assets have long lives, and they impact rates for decades.
- Rate of return (r) must be comparable to other market opportunities with similar risk for the investor and is a weighted combination of the cost of equity and the cost of debt.
- Expenses (E) must be prudent.
- In addition to the RR amount, most utilities also receive automatic adjustments to some major expenses, such as fuel, reflecting significant changes in costs.