EL PASO ELECTRIC CO /TX/
Form 10-Q
November 02, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q
(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2018
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _______ to _______
Commission file number: 001-14206
El Paso Electric Company
(Exact name of registrant as specified in its charter)

Texas	74-0607870
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
Stanton Tower, 100 North Stanton, El Paso, Texas	79901
(Address of principal executive offices)	(Zip Code)

(915) 543-5711
(Registrant's telephone number, including area code)
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES x NO o
Indicate by check mark whether the registrant has submitted electronically, every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). YES x NO o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	x	Accelerated filer	o
Non-accelerated filer	o	Smaller reporting company	o
		Emerging growth company	o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES o NO x

As of October 31, 2018, there were 40,691,951 shares of the Company's no par value common stock outstanding.

DEFINITIONS

The following abbreviations, acronyms or defined terms used in this report are defined below:

Abbreviations, Acronyms or Defined Terms	Terms
A&G	Administrative and general
ABFUDC	Allowance for Borrowed Funds Used During Construction
ACE	Affordable Clean Energy
AEFUDC	Allowance for Equity Funds Used During Construction
AFUDC	Allowance for Funds Used During Construction
ANPP Participation Agreement	Arizona Nuclear Power Project Participation Agreement dated August 23, 1973, as amended
AOCI	Accumulated Other Comprehensive Income
APS	Arizona Public Service Company
ARO	Asset Retirement Obligations
ASC	Accounting Standards Codification
ASU	Accounting Standards Update
CAA	Clean Air Act
CCN	Certificate of Convenience and Necessity
Company	El Paso Electric Company
CPP	Clean Power Plan
CWIP	Construction Work In Progress
DOE	U.S. Department of Energy
El Paso	City of El Paso, Texas
EPA	The U.S. Environmental Protection Agency
Exchange Act	The Securities Exchange Act of 1934, as amended
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
Four Corners	Four Corners Generating Station
FPPCAC	New Mexico Fuel and Purchased Power Cost Adjustment Clause
GAAP	U.S. Generally Accepted Accounting Principles
GHG	Greenhouse Gas
HAFB	Holloman Air Force Base
IRS	U.S. Internal Revenue Service
kW	Kilowatt(s)
kWh	Kilowatt-hour(s)
Las Cruces	City of Las Cruces, New Mexico
MPS	The Company's Montana Power Station
MW	Megawatt(s)
MWh	Megawatt-hour(s)
NAAQS	National Ambient Air Quality Standards
NAV	Net Asset Value
Newman	The Company's Newman Power Station
NDT	The Company's Palo Verde nuclear decommissioning trust funds
NMPRC	New Mexico Public Regulation Commission
NMPRC Final Order	NMPRC Final Order in Case No. 15-00127-UT
NOL carryforwards	Net Operating Loss carryforwards

(i)

Abbreviations, Acronyms or Defined Terms	Terms
OATT	Open Access Transmission Tariff
O&M	Operations and maintenance
Palo Verde	Palo Verde Generating Station
Ppb	Parts Per Billion
PUCT	Public Utility Commission of Texas
RCF	The Company's Revolving Credit Facility
RGEC	Rio Grande Electric Cooperative
RGRT	Rio Grande Resources Trust II
Rio Grande	The Company's Rio Grande Power Station
SAB 118	SEC Staff Accounting Bulletin No. 118
SEC	U.S. Securities and Exchange Commission
Securities Act	The Securities Act of 1933, as amended
TCJA	The federal legislation commonly referred to as the Tax Cuts and Jobs Act of 2017
Texas Fuel Rule	Texas fuel cost recovery rule
U.S.	United States
2016 PUCT Final Order	PUCT Final Order in Docket No. 44941
2017 Form 10-K	Annual Report of El Paso Electric Company on Form 10-K for the fiscal year ended December 31, 2017
2017 PUCT Final Order	PUCT Final Order in Docket No. 46831

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

EL PASO ELECTRIC COMPANY
BALANCE SHEETS

	September 30, 2018 (Unaudited)	December 31, 2017
ASSETS		
(In thousands)		
Utility plant:		
Electric plant in service	$ 4,089,896	$ 3,982,095
Less accumulated depreciation and amortization	(1,375,721)	(1,320,175)
Net plant in service	2,714,175	2,661,920
Construction work in progress	207,514	146,059
Nuclear fuel; includes fuel in process of $70,778 and $59,689, respectively	205,991	194,933
Less accumulated amortization	(82,840)	(74,475)
Net nuclear fuel	123,151	120,458
Net utility plant	3,044,840	2,928,437
Current assets:		
Cash and cash equivalents	15,965	6,990
Accounts receivable, principally trade, net of allowance for doubtful accounts of $2,275 and $2,300, respectively	117,950	88,585
Inventories, at cost	53,078	50,910
Prepayments and other	13,838	10,307
Total current assets	200,831	156,792
Deferred charges and other assets:		
Decommissioning trust funds	297,030	286,866
Regulatory assets	83,764	96,036
Other	17,728	16,232
Total deferred charges and other assets	398,522	399,134
Total assets	$ 3,644,193	$ 3,484,363

See accompanying notes to financial statements.

EL PASO ELECTRIC COMPANY
BALANCE SHEETS (Continued)

	September 30, 2018 (Unaudited)	December 31, 2017
CAPITALIZATION AND LIABILITIES		
(In thousands except for share data)		
Capitalization:		
Common stock, stated value $1 per share, 100,000,000 shares authorized, 65,672,747 and 65,694,829 shares issued, and 155,941 and 133,859 restricted shares, respectively	$ 65,829	$ 65,829
Capital in excess of stated value	327,320	326,117
Retained earnings	1,257,397	1,159,667
Accumulated other comprehensive income (loss), net of tax	(34,633)	11,058
	1,615,913	1,562,671
Treasury stock, 25,136,737 and 25,244,350 shares, respectively, at cost	(418,713)	(420,506)
Common stock equity	1,197,200	1,142,165
Long-term debt, net of current portion	1,385,254	1,195,988
Total capitalization	2,582,454	2,338,153
Current liabilities:		
Short-term borrowings under the revolving credit facility	19,362	173,533
Accounts payable, principally trade	73,537	59,270
Taxes accrued	42,054	35,660
Interest accrued	20,961	12,470
Over-collection of fuel revenues, regulatory liability	9,905	6,225
Other	38,252	29,067
Total current liabilities	204,071	316,225
Deferred credits and other liabilities:		
Accumulated deferred income taxes	325,383	305,023
Accrued pension liability	77,261	83,838
Accrued post-retirement benefit liability	28,130	26,417
Asset retirement obligation	99,144	93,029
Regulatory liabilities	299,431	296,685
Other	28,319	24,993
Total deferred credits and other liabilities	857,668	829,985
Commitments and contingencies		
Total capitalization and liabilities	$ 3,644,193	$ 3,484,363

See accompanying notes to financial statements.

EL PASO ELECTRIC COMPANY
STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands except for share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Operating revenues	$300,271	$297,470	$712,780	$720,648
Operating expenses:				
Fuel and purchased power	71,086	75,319	176,737	191,492
Operations and maintenance	83,355	74,685	252,370	236,145
Depreciation and amortization	24,169	22,565	71,941	66,994
Taxes other than income taxes	21,728	21,213	54,616	54,208
	200,338	193,782	555,664	548,839
Operating income	99,933	103,688	157,116	171,809
Other income (deductions):				
Allowance for equity funds used during construction	824	668	2,462	2,209
Investment and interest income, net	16,815	8,989	33,042	30,308
Miscellaneous non-operating income	3,037	3,075	9,245	8,867
Miscellaneous non-operating deductions	(3,263)	(3,180)	(8,775)	(8,677)
	17,413	9,552	35,974	32,707
Interest charges (credits):				
Interest on long-term debt and revolving credit facility	19,603	18,215	55,785	54,989
Other interest	4,127	4,673	13,896	13,746
Capitalized interest	(1,488)	(1,193)	(4,067)	(3,831)
Allowance for borrowed funds used during construction	(881)	(671)	(2,551)	(2,173)
	21,361	21,024	63,063	62,731
Income before income taxes	95,985	92,216	130,027	141,785
Income tax expense	22,714	32,532	30,427	50,024
Net income	$73,271	$59,684	$99,600	$91,761
Basic earnings per share	$1.80	$1.47	$2.45	$2.26
Diluted earnings per share	$1.79	$1.47	$2.44	$2.26
Dividends declared per share of common stock	$0.360	$0.335	$1.055	$0.980
Weighted average number of shares outstanding	40,535,489	40,427,589	40,514,961	40,408,100
Weighted average number of shares and dilutive potential shares outstanding	40,697,047	40,551,315	40,644,493	40,516,777

See accompanying notes to financial statements.

EL PASO ELECTRIC COMPANY
STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands except for share data)

	Twelve Months Ended September 30,	
	2018	2017
Operating revenues	$908,929	$908,685
Operating expenses:		
Fuel and purchased power	229,996	245,425
Operations and maintenance	336,506	315,677
Depreciation and amortization	95,790	88,214
Taxes other than income taxes	71,271	69,444
	733,563	718,760
Operating income	175,366	189,925
Other income (deductions):		
Allowance for equity funds used during construction	3,278	3,365
Investment and interest income, net	41,587	39,281
Miscellaneous non-operating income	12,428	11,901
Miscellaneous non-operating deductions	(11,677)	(11,542)
	45,616	43,005
Interest charges (credits):		
Interest on long-term debt and revolving credit facility	73,766	73,312
Other interest	18,320	17,757
Capitalized interest	(5,258)	(5,083)
Allowance for borrowed funds used during construction	(3,353)	(2,992)
	83,475	82,994
Income before income taxes	137,507	149,936
Income tax expense	31,407	52,519
Net income	$106,100	$97,417
Basic earnings per share	$2.61	$2.40
Diluted earnings per share	$2.60	$2.40
Dividends declared per share of common stock	$1.39	$1.29
Weighted average number of shares outstanding	40,494,482	40,398,022
Weighted average number of shares and dilutive potential shares outstanding	40,630,758	40,498,642

See accompanying notes to financial statements.

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EL PASO ELECTRIC COMPANY
STATEMENTS OF COMPREHENSIVE OPERATIONS
(Unaudited)
(In thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,		Twelve Months Ended September 30,	
	2018	2017	2018	2017	2018	2017
Net income	$73,271	$59,684	$99,600	$91,761	$106,100	$97,417
Other comprehensive income (loss):						
Unrecognized pension and post-retirement benefit costs:						
Net gain (loss) arising during period	—	—	—	—	12,634	(20,053)
Prior service benefit	—	—	—	—	—	32,697
Reclassification adjustments included in net income for amortization of:						
Prior service benefit	(2,413)	(2,414)	(7,243)	(7,243)	(9,657)	(9,657)
Net loss	1,640	1,695	4,790	5,083	6,483	6,516
Net unrealized gains/losses on marketable securities:						
Net holding gains (losses) arising during period	(948)	5,945	(4,909)	18,124	2,242	17,275
Reclassification adjustments for net (gains) losses included in net income	443	(1,765)	1,108	(9,122)	(396)	(11,192)
Net losses on cash flow hedges:						
Reclassification adjustment for interest expense included in net income	144	134	423	396	559	523
Total other comprehensive income (loss) before income taxes	(1,134)	3,595	(5,831)	7,238	11,865	16,109
Income tax benefit (expense) related to items of other comprehensive income (loss):						
Unrecognized pension and post-retirement benefit costs	174	262	520	716	(3,811)	(3,539)
Net unrealized (gains) losses on marketable securities	105	(825)	761	(1,814)	(347)	(1,163)
Losses on cash flow hedges	(32)	(49)	(113)	(174)	(162)	(220)
Total income tax benefit (expense)	247	(612)	1,168	(1,272)	(4,320)	(4,922)
Other comprehensive income (loss), net of tax	(887)	2,983	(4,663)	5,966	7,545	11,187
Comprehensive income	$72,384	$62,667	$94,937	$97,727	$113,645	$108,604

See accompanying notes to financial statements.

EL PASO ELECTRIC COMPANY
STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	Nine Months Ended September 30, 2018		2017	
Cash flows from operating activities:				
Net income	$ 99,600		$ 91,761	
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization of electric plant in service	71,941		66,994	
Amortization of nuclear fuel	29,822		32,494	
Deferred income taxes, net	24,369		47,457	
Allowance for equity funds used during construction	(2,462	)	(2,209	)
Other amortization and accretion	15,427		14,934	
Net gains on decommissioning trust funds	(9,683	)	(9,122	)
Other operating activities	31		(762	)
Change in:				
Accounts receivable	(33,958	)	(39,298	)
Inventories	(1,480	)	(2,988	)
Prepayments and other	(5,716	)	(5,120	)
Accounts payable	4,920		525	
Taxes accrued	7,632		6,539	
Interest accrued	8,491		5,741	
Net over-collection of fuel revenues	3,680		13,888	
Other current liabilities	9,185		(138	)
Deferred charges and credits	(321	)	(1,950	)
Net cash provided by operating activities	221,478		218,746	
Cash flows from investing activities:				
Cash additions to utility property, plant and	(171,433	)	(148,436	)

equipment				
Cash additions to nuclear fuel	(28,769	)	(31,618	)
Insurance proceeds received for equipment	5,351		8,069	
Capitalized interest and AFUDC:				
Utility property, plant and equipment	(5,013	)	(4,382	)
Nuclear fuel and other	(4,067	)	(3,831	)
Allowance for equity funds used during construction	2,462		2,209	
Decommissioning trust funds:				
Purchases, including funding of $1.6 million and $3.4 million, respectively	(74,438	)	(80,785	)
Sales and maturities	70,156		76,498	
Other investing activities	3,639		(204	)
Net cash used for investing activities	(202,112	)	(182,480	)
Cash flows from financing activities:				
Dividends paid	(42,898	)	(39,747	)
Borrowings under the revolving credit facility:				
Proceeds	504,707		532,332	
Payments	(658,878	)	(446,005	)
Proceeds from issuance of senior notes	125,000		—	
Proceeds from issuance of RGRT senior notes	65,000		—	
Payment on maturing senior notes	—		(50,000	)
Payment on maturing pollution control bonds	—		(33,300	)
Other financing activities	(3,322	)	(906	)
Net cash used for financing activities	(10,391	)	(37,626	)
Net increase (decrease) in cash and cash equivalents	8,975		(1,360	)
Cash and cash equivalents at beginning of period	6,990		8,420	
Cash and cash equivalents at end of period	$ 15,965		$ 7,060	

See accompanying notes to financial statements.

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EL PASO ELECTRIC COMPANY
NOTES TO FINANCIAL STATEMENTS
(Unaudited)

A. Principles of Preparation

These condensed financial statements should be read in conjunction with the financial statements and notes thereto in the Annual Report of El Paso Electric Company on Form 10-K for the fiscal year ended December 31, 2017 ("2017 Form 10-K"). Capitalized terms used in this report and not defined herein have the meaning ascribed to such terms in the 2017 Form 10-K. In the opinion of the Company's management, the accompanying financial statements contain all adjustments necessary to present fairly the financial position of the Company at September 30, 2018 and December 31, 2017; the results of its operations and comprehensive operations for the three, nine and twelve months ended September 30, 2018 and 2017; and its cash flows for the nine months ended September 30, 2018 and 2017. The results of operations and comprehensive operations for the three and nine months ended September 30, 2018 and 2017, and the cash flows for the nine months ended September 30, 2018 and 2017, are not necessarily indicative of the results to be expected for the full calendar year.

Pursuant to the rules and regulations of the United States ("U.S.") Securities Exchange Commission ("SEC"), certain financial information has been condensed and certain footnote disclosures have been omitted. Such information and disclosures are normally included in financial statements prepared in accordance with U.S. Generally Accepted Accounting Principles ("GAAP").

Reclassification. Certain amounts in the financial statements for 2017 have been reclassified to conform with the 2018 presentation. The Company implemented Accounting Standards Update ("ASU") 2017-07, Compensation - Retirement Benefits, and ASU 2016-15, Statement of Cash Flows, in the first quarter of 2018, retrospective to all periods presented in the Company's financial statements. See "New Accounting Standards Adopted" below for further details.

Use of Estimates. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company evaluates its estimates on an on-going basis, including those related to depreciation, unbilled revenue, income taxes, fuel costs, pension and other post-retirement obligations and asset retirement obligations ("AROs"). Actual results could differ from those estimates.

Revenues. The Company recognizes revenue associated with contracts with customers when performance obligations under the terms of the contract with the customer are satisfied. Revenue is measured as the amount of consideration the Company receives in exchange for transferring goods or providing services to the customer. Taxes collected concurrently with revenue producing activities are excluded from revenue. Unbilled revenues are recorded for estimated amounts of energy delivered in the period following the customer's last billing cycle to the end of the reporting period. Unbilled revenues are estimated based on monthly generation volumes and by applying an average revenue/kilowatt-hour ("kWh") to the number of estimated kWhs delivered but not billed. Accounts receivable included accrued unbilled revenues of $31.0 million at September 30, 2018 and $22.2 million at December 31, 2017. The Company presents revenues net of sales taxes in its statements of operations.

Depreciation. The Company routinely evaluates the depreciable service lives, cost of removal and salvage values of its property, plant and equipment. Depreciation is provided on a straight-line basis over the estimated remaining lives of the assets (ranging in average from 5 to 48 years). When property subject to composite depreciation is retired or otherwise disposed of in the normal course of business, its cost together with the cost of removal, less salvage is charged to accumulated depreciation. For other property dispositions, the applicable cost and accumulated depreciation is removed from the balance sheet accounts and a gain or loss is recognized.

New Accounting Standards Adopted

In March 2016, the Financial Accounting Standards Board ("FASB") issued ASU 2016-09, Compensation - Stock Compensation (Topic 718) Improvements to Employee Share-Based Payment Accounting, to simplify the accounting for share-based payment transactions, including the income tax consequences, classification of awards either as equity or liabilities, and classification on the statements of cash flows. The Company adopted the new standard effective January 1, 2017. The adoption of the new standard did not have a material impact on the Company’s financial condition, results of operations or cash flows. The cumulative effect of the adoption of the new standard was to increase net operating loss carryforward ("NOL carryforward") deferred tax assets and retained earnings by $0.2 million on January 1, 2017.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), to provide a framework that replaces the existing revenue recognition guidance, and has since modified the standard with several ASUs. The standard provides that an entity should recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. On January 1, 2018, the Company adopted the new accounting standard using the modified retrospective method. There was no cumulative effect adjustment at the initial application of the new standard. In addition, comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. The Company expects the ongoing impact of the new standard to be immaterial to net income. As required by the standard, revenues of $5.9 million related to reimbursed costs of energy efficiency programs approved by the Company's regulators are reported in year-to-date operating revenues from customers prospectively, as opposed to being offset with associated costs within operations and maintenance. Related expenses of an equal amount are reported in operations and maintenance expenses. See Note B, Revenues, for additional information.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Liabilities, to enhance the reporting model for financial instruments by addressing certain aspects of recognition, measurement, presentation and disclosure. The Company adopted the new standard effective January 1, 2018. The adoption of ASU 2016-01 eliminates the requirements to classify investments in equity securities with readily determinable fair values into trading or available for sale and requires entities to measure equity investments at fair value and recognize any changes in fair value in the Statements of Operations. ASU 2016-01 requires a modified retrospective approach and therefore comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. Upon adoption of the new standard, the Company recorded a cumulative effect adjustment, net of income taxes, to increase retained earnings by $41.0 million with an offset to accumulated other comprehensive income ("AOCI"). In addition, the Company recorded net gains of $3.7 million related to equity securities still held at September 30, 2018. In March 2018, the FASB issued ASU 2018-04, Investments - Debt Securities (Topic 320) and Regulated Operations (Topic 980), which provides clarification to ASU 2016-01.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230) Classification of Certain Cash Receipts and Cash Payments, to reduce diversity in practice in how certain cash receipts and cash payments are classified in the statement of cash flows. The Company adopted the new standard effective January 1, 2018. ASU 2016-15 was applied using a retrospective transition method to each period presented. Accordingly, the Company presented in the Statement of Cash Flows insurance proceeds received for equipment of $5.4 million and $8.1 million, respectively, for the nine months ended September 30, 2018 and 2017 as cash inflows from investing activities.

In March 2017, the FASB issued ASU 2017-07, Compensation-Retirement Benefits (Topic 715) Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. ASU 2017-07 amends Accounting Standards Codification ("ASC") 715, Compensation - Retirement Benefits, to require companies to present the service cost component of net benefit cost in the income statement line items where compensation cost is reported. Companies will present all other components of net benefit cost separately from the line item(s) that includes the service cost and outside of any subtotal of operating income. In addition, only the service cost component will be eligible for capitalization in assets. The Company adopted the new standard effective January 1, 2018. The amendments in ASU 2017-07 were applied retrospectively for the income statement presentation of the service cost component and the other components of net benefit costs. The Company elected to apply the practical expedient and used the amounts disclosed in its pension and other postretirement benefit plan note for the 2017 comparative period as the estimation basis for applying the retrospective presentation requirements. See Note J, Employee Benefits, for additional information.

In March 2018, the FASB issued ASU 2018-05, Income Taxes (Topic 740) Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118 ("SAB 118"), to add various SEC paragraphs for clarification due to the federal legislation commonly referred to as the Tax Cuts and Jobs Act of 2017 ("TCJA"). The Company adopted ASU 2018-05 upon issuance and implemented SAB 118 in December of 2017 in conjunction with the enactment of the TCJA.

In August 2018, the FASB issued ASU 2018-15, Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract (Topic 350). ASU 2018-15 aligns the requirements for capitalizing implementation costs for a cloud computing arrangement with the requirements for capitalizing implementation costs for an internal use software license. Implementation costs for a cloud computing arrangement will be capitalized or expensed based on the nature of the costs and the project's stage in which they are incurred by applying the existing guidance for internal use software implementation costs. Capitalized costs for a cloud computing arrangement will be presented on the same line of the balance sheet as any related prepaid amounts for the arrangement, while amortization of those costs will be presented on the same line of the income statement as the related hosting fees. Early adoption is permitted, and entities may apply the guidance either prospectively to eligible costs incurred on or after the effective date or retrospectively. The Company early-adopted this guidance in the third quarter of 2018, on a prospective basis, and the adoption did not have a material impact on the Company's financial condition, results of operations or cash flows.

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EL PASO ELECTRIC COMPANY
NOTES TO FINANCIAL STATEMENTS
(Unaudited)

New Accounting Standards to be Adopted in the Future

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and requiring qualitative and quantitative disclosures on leasing agreements. ASU 2016-02 maintains a distinction between finance leases and operating leases similar to the distinction under previous lease guidance for capital leases and operating leases. The impact of leases reported in the Company's operating results and statement of cash flows is expected to be similar to previous GAAP. ASU 2016-02 requires the recognition in the statement of financial position, by the lessee, of a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. How leases are recorded in regard to financial position represents a significant change from previous GAAP guidance. The lessee is permitted to make an accounting policy election to not recognize lease assets and lease liabilities for short-term leases. Adoption of the new lease accounting standard will require the Company to apply the new standard to the earliest period using a modified retrospective approach. The Company continues to monitor activities of the FASB, including the impact of ASU 2018-01, Land Easement Practical expedient for Transition to Topic 842, ASU 2018-11, Targeted Improvements, and the proposed update related to narrow scope improvements for lessors. ASU 2018-11 allows entities to adopt the standard with a cumulative effect adjustment as of the beginning of the adoption year, while maintaining prior year comparative financial information and disclosures as reported. ASU 2018-01 provides an optional practical expedient to not evaluate existing or expired land easements under Topic 842, if those land easements were not previously accounted for as leases under ASC Topic 840. The Company currently anticipates that it will apply the practical expedient under ASU 2018-01 to its existing or expired land easements as part of its transition to Topic 842. The Company's implementation process is continuing and includes finalizing the following activities: the analysis of the Company's lease population, the implementation of a new lease accounting system, the determination of the transition method and practical expedients that will be applied, and evaluating the impact, if any, on changes to business processes, systems and controls to support recognition and disclosure under the new guidance. The Company will adopt this guidance effective January 1, 2019.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326). ASU 2016-13 changes how companies measure and recognize credit impairment for many financial assets. The new expected credit loss model will require companies to immediately recognize an estimate of credit losses expected to occur over the remaining life of the financial assets that are in the scope of the standard. The ASU also makes targeted amendments to the current impairment model for available-for-sale debt securities. ASU 2016-13 will be required for reporting periods beginning after December 15, 2019. ASU 2016-13 will be applied in a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is implemented. The Company is currently assessing the future impact of ASU 2016-13.

In February 2018, the FASB issued ASU 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220), as a result of concerns raised due to the TCJA. More specifically, because the remeasurement of deferred taxes due to the change in the federal corporate income tax rate is required to be included in income from continuing operations, the tax effects of items within AOCI (referred to as stranded tax effects) do not reflect the appropriate tax rate. ASU 2018-02 generally allows companies to reclassify stranded taxes from AOCI to retained earnings. The amount of the adjustment would be the difference between the historical federal corporate income tax rate of 35% and the newly enacted 21% federal corporate income tax rate. The provisions of ASU 2018-02 are effective for fiscal years and interim periods within that reporting period beginning after December 15, 2018. Early adoption is permitted, including adoption in any interim periods for reporting periods for which financial statements have not been issued. The Company is currently evaluating the impact of ASU 2018-02 and its impact on regulated utilities. At September 30, 2018, stranded taxes in AOCI are approximately $7.2 million.

EL PASO ELECTRIC COMPANY
NOTES TO FINANCIAL STATEMENTS
(Unaudited)

Supplemental Cash Flow Disclosures (in thousands)

	Nine Months Ended September 30,	
	2018	2017
Cash paid for:		
Interest on long-term debt and borrowings under the revolving credit facility	$47,479	$47,412
Income tax paid, net	2,480	1,576
Non-cash investing and financing activities:		
Changes in accrued plant additions	9,347	(6,228)
Grants of restricted shares of common stock	1,030	1,171
Issuance of performance shares	1,499	932

B. Revenues

On January 1, 2018, the Company adopted ASU 2014-09, Revenue from Contracts with Customers (Topic 606), for all of its contracts using the modified retrospective method. There was no cumulative effect adjustment at the initial application of the new standard. In addition, comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. The Company expects the ongoing impact of the new standard to be immaterial to net income and no significant changes in the Company's business processes and internal controls were necessary upon adoption of the new standard.
The following table disaggregates revenue from contracts with customers, for the three, nine and twelve months ended September 30, 2018 (in thousands):
September