

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Disposition of gross-up
funds collected by Hydratech
Utilities, Inc. in Martin
County.

DOCKET NO. 980504-WS
ORDER NO. PSC-98-0750-AS-WS
ISSUED: June 1, 1998

The following Commissioners participated in the disposition of this matter:

JULIA L. JOHNSON, Chairman
J. TERRY DEASON
SUSAN F. CLARK
JOE GARCIA
E. LEON JACOBS, JR.

NOTICE OF PROPOSED AGENCY ACTION ORDER ACCEPTING SETTLEMENT OFFER
AND REQUIRING NO REFUND FOR THE YEAR 1996

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service Commission that the action discussed herein is preliminary in nature and will become final unless a person whose interests are substantially affected files a petition for a formal proceeding, pursuant to Rule 25-22.029, Florida Administrative Code.

BACKGROUND

Hydratech Utilities, Inc. (Hydratech or utility), is a Class A water and wastewater utility providing service to approximately 5,301 water and 4,499 wastewater customers in Martin County. According to its 1996 annual report, the utility reported gross operating revenues of \$1,330,262 and \$1,058,728 for water and wastewater, respectively, and net operating income of \$182,542 for water and net operating income of \$793 for wastewater.

As a result of the repeal of Section 118(b) of the Internal Revenue Code, effective January 1, 1987, contributions-in-aid-of-construction (CIAC) became gross income and were depreciable for federal tax purposes. Therefore, by Order No. 16971, issued December 18, 1986, we authorized corporate utilities to collect the gross-up on CIAC in order to meet the tax impact resulting from the inclusion of CIAC as gross income.

DOCUMENT NUMBER-DATE

05867 JUN-1 98

TRAC-RETURNS/REPORTING

Orders Nos. 16971 and 23541, issued December 18, 1986 and October 1, 1990, respectively, require that utilities annually file information which would be used to determine the actual state and federal income tax liability directly attributable to the CIAC. The information would also determine whether refunds of gross-up would be appropriate. These orders also required that all gross-up collections for a tax year, which are in excess of a utility's actual tax liability for the same year, should be refunded on a pro rata basis to those persons who contributed the taxes.

However, the Small Business Job Protection Act of 1996 (The Act), which became law on August 20, 1996, provided for the non-taxability of CIAC collected by water and wastewater utilities effective retroactively for amounts received after June 12, 1996.

The disposition of gross-up funds collected by the utility for 1995 was handled in Docket No. 970275-WS, Order No. PSC-97-0816-FOF-WS, issued July 7, 1997. The purpose of this Order is to address the disposition of gross-up funds collected by the utility for 1996.

REFUND REQUIREMENT

In compliance with Orders Nos. 16971 and 23541, Hydratech filed its 1996 annual CIAC report regarding its collection of gross-up. The utility calculated its above-the-line income to be \$888,384. We have adjusted the utility's above-the-line income by \$20,236 to reflect first year's depreciation as above-the-line. Therefore, we calculate the above-the-line income to be \$868,148.

Based upon the foregoing, we have calculated the gross-up required to pay the tax liability resulting from the collection of taxable CIAC by grossing-up the net taxable CIAC amount, in accordance with the method adopted in Order No. PSC-92-0961-FOF-WS. Our calculations, taken from the information provided by the utility in its gross-up report filed for 1996, are reflected on Schedule No. 1.

The utility's 1996 CIAC report indicates that the utility was in a taxable position on an above-the-line basis prior to the inclusion of taxable CIAC and gross-up. Therefore, all of the taxable CIAC received would be taxed. The report indicates a total of \$528,355 in taxable CIAC was received, with \$20,236 being deducted for the first year's depreciation. Using the 37.63 percent combined marginal federal and state tax rate as provided in

the 1996 CIAC Report, we calculate the income tax effect to be \$191,205. When this amount is multiplied by the expansion factor for gross-up taxes, the amount of gross-up required to pay the tax effect on the CIAC is calculated to be \$306,566. The utility collected \$309,258 of gross-up monies. Therefore, the utility collected \$2,692 more in gross-up than was required to pay the tax impact.

The utility has requested that it be allowed to offset 50 percent of the legal and accounting costs directly associated with preparing the required reports and calculating the tax effect. We have considered on several occasions, the question of whether an offset should be allowed pursuant to the orders governing CIAC gross-up. In Dockets Nos. 961076-WS, and 970275-WS, by Orders Nos. PSC-97-0657-AS-WS and PSC-97-0816-FOF-WS, respectively, we accepted the utility's settlement proposals that 50 percent of the legal and accounting costs be offset against the refund amount. In general, the utility argues that the legal and accounting costs should be deducted from the amount of the contributors' refund, as the contributors are the cost-causers and as such, those costs should be recovered from the cost-causers.

As in the cases cited above, we find that acceptance of the utility's request would avoid the substantial costs associated with a hearing, which may in fact exceed the amount of the legal and accounting costs to be recovered. We also note that the actual costs associated with implementing the refunds have not been included in these calculations and will be absorbed by the utility. Moreover, we believe the utility's request is a reasonable "middle ground". Therefore, while not adopting the utility's position, we will accept Hydratech's offer of settlement and allow it to offset 50 percent of the legal and accounting fees against the refund.

The utility has provided documentation showing legal and accounting fees of \$6,914. A review of these fees shows that they are all directly associated with preparing the required reports and calculating the tax effect, and, thus, are considered to be legitimate expenses. Fifty percent of this amount is \$3,457; however, only \$2,692 of this amount is needed to offset the over collection of \$2,692. When the legal and accounting fees of \$2,692 are offset against the over collection of \$2,692, there is nothing left to refund, and no refunds are required for 1996.

CLOSING OF DOCKET

Upon expiration of the protest period, if a timely protest is not received from a substantially affected person, this docket shall be closed.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the request of Hydratech Utilities, Inc., to offset fifty percent of the legal and accounting fees against any over collections is accepted. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, shall become final and effective unless an appropriate petition, in the form provided by Rule 25-22.036, Florida Administrative Code, is received by the Director, Division of Records and Reporting, 2540 Chambered Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings or Judicial Review" attached hereto. It is further

ORDERED that no refunds are required for the collection of gross-up on contributions-in-aid-of-construction for the year 1996. It is further

ORDERED that the schedule attached to this Order is incorporated into and made a part of this Order. It is further

ORDERED that in the event this Order becomes final, this Docket shall be closed.

By ORDER of the Florida Public Service Commission this 1st day of June, 1998.

BLANCA S. BAYÓ, Director
Division of Records and Reporting



Kay Flynn, Chief
Bureau of Records

(S E A L)

RRJ/LAJ

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

The action proposed herein is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25-22.029(4), Florida Administrative Code, in the form provided by Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 2540 Chambered Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on June 22, 1998.

In the absence of such a petition, this order shall become effective on the day subsequent to the above date as provided by Rule 25-22.029(6), Florida Administrative Code.

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

If this order becomes final and effective on the date described above, any party substantially affected may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or by the First District Court of Appeal in the case of a water or wastewater utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days of the effective date of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

COMMISSION CALCULATED GROSS-UP REFUND

Hydratech Utilities, Inc.

SOURCE: (Line references are from CIAC Reports)

		1996
		-
1 Form 1120, Line 30 (Line 15)	\$	868,148
2 Less CIAC (Line 7)		(528,355)
3 Less Gross-up Collected (Line 10)		(309,258)
4 Add First Year's Depr on CIAC (Line 8)		20,236
5 Add/Less Other Effects (Lines 20 & 21)		-
6		-
7 Adjusted Income Before CIAC and Gross-up	\$	50,771
8		-
9 Taxable CIAC (Line 7)	\$	528,355
10 Less first years depr. (Line 8)	\$	(20,236)
11		-
12 Adjusted Income After CIAC	\$	558,890
13 Less: NOL Carry Forward	\$	0
14		-
15 Net Taxable CIAC	\$	508,119
16 Combined Marginal state & federal tax rates		37.63%
17		-
18 Net Income tax on CIAC	\$	191,205
19 Less ITC Realized		0
20		-
21 Net Income Tax	\$	191,205
22 Expansion Factor for gross-up taxes		1.60333493666827
23		-
24 Gross-up Required to pay tax effect	\$	306,566
25 Less CIAC Gross-up collected (Line 19)		(309,258)
26		-
27 (OVER) OR UNDER COLLECTION	\$	(2,692)
28		=
29 TOTAL YEARLY REFUND	\$	(2,692)
30 Offset of Legal and Accounting Fees	\$	3,019
31		-----
32	\$	327
33		==
34 PROPOSED REFUND (excluding interest)	\$	0
		=