ORIGINAL

M E M O R A N D U M

August 21, 1998

TO: DIVISION OF RECORDS AND REPORTING

FROM: DIVISION OF LEGAL SERVICES (JAEGER)

RE: DOCKET NO. 931065-WS - DISPOSITION OF CONTRIBUTIONS-IN-AID- OF CONSTRUCTION (CIAC) FUNDS RECEIVED BY MARTIN DOWNS UTILITIES, INC. IN MARION COUNTY DURING 1990, 1991, 1992, AND 1993.

Please place the attached Summons and Petition, which were filed in Martin County Circuit Court, in the docket file.

RRJ/lw

Attachment

cc: Division of Water and Wastewater (Iwenjiora)

ACK ____
AFA ____
APP ____
CAF ____
CMU ____
CTR ____
EAG ____
LEG ____
LIN ____
OPC ____
RCH ____
SEC 1
WAS ____
OTH ____

IN THE CIRCUIT COURT OF THE
NINETEENTH JUDICIAL CIRCUIT,
MARTIN COUNTY

STATE OF FLORIDA

PUBLIC SERVICE COMMISSION
Plaintiff.

VS.
MARTIN DOWNS UTILITIES, INC.
Defendant.

CASE NO._____

Summons

PERSONAL SERVICE ON A NATURAL PERSON

TO: Steve Fry
Peter Cummings and Associates
3501 Southwest Corporate Parkway
Palm City, Florida 32302-1567

IMPORTANT

A lawsuit has been filed against you in this court. You have 20 calendar days after receiving this summons to file your written response to the attached complaint. This response must be filed with the clerk of the court at the address shown below.

If you do not file your response on time, you may lose your case. (The court could enter a judgment in favor of the plaintiff and you could lose wages, money and property without further warning.)

You may want to contact an attorney right away, as court proceedings can get involved and advise of counsel could be very important to you. If you do not know an attorney, you may call an attorney referral service or a legal aid office listed in the telephone directory. If you do not hire an attorney and chose to represent yourself in court, make sure that your response contains the case number and the names of the parties (as shown at the top of this page).

The original of your response must be filed with:

Clerk of the Circuit Court
Civil Division
100 E. Ocean Blvd.
Stuart, Florida 34994

P.O. Drawer 9016
Stuart, Florida 34995

A copy of your response must also be mailed or delivered to the plaintiff's attorney:

- Ralph R. Jaeger, Senior Attorney
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

Remember to keep a copy of your response for your own referral.

THE STATE OF FLORIDA
TO EACH SHERIFF OF THE STATE: You are commanded to serve this Summons and a copy of the Complaint in this lawsuit on the above-named defendant(s).

DATED ON _____, 19 _____.

MARSHA STILLER
CLERK OF THE CIRCUIT COURT

By: _____
Deputy Clerk

CCC - 206

IMPORTANTE

Un pleito ha sido archivado en su contra en ésta corte. Usted tiene 20 días hábiles después de recibir ésta citación, para archivar su respuesta por escrito a ésta queja. Esta respuesta debe ser archivada con el Secretario de la Corte en la dirección mostrada abajo.

Si Usted no archiva su respuesta a tiempo, Usted quizás pierda su caso. (La Corte entrará un juicio en favor del demandador, y Usted perderá su salario, dinero y propiedad sin previo aviso).

Usted tal vez quiera ponerse en contacto con su abogado inmediatamente, como procedimiento, la Corte le aconseja que un abogado sería de mucha importancia para Usted. Si Usted no conoce ningún abogado, usted puede llamar al servicio referente de abogados, o a cualquier oficina legal citada en el directorio telefónico. Si usted no emplea un abogado, y desea representarse a si mismo en la Corte, asegúrese de que su respuesta contiene el número de su caso y los nombres de los participantes, (como mostrado en la parte superior de este documento).

El documento original de su respuesta debe ser archivado con:

Clerk of the Circuit Court
Civil Division
100 E. Ocean Blvd.
Stuart, Florida 34994

P.O. Drawer 9016
Stuart, Florida 34995

Una copia de su respuesta debe ser enviada a el abogado del demandador perteneciente al nombre y direccion mostrado al lado de el asterisco en la parte de atras.

Recuerde conservar una copia de la misma, para su propio beneficio.

IMPORTANT

Une demande de procès a été déposée contre vous à ce tribunal. Vous avez 20 jours après la réception de cette sommation pour déposer votre réponse écrite à la plainte ci-jointe. Cette réponse doit être déposée auprès du greffier du tribunal à l'adresse mentionnée ci-dessous.

Si vous ne soumettez pas votre réponse à temps, il est possible que vous perdiez le procès. (Le tribunal pourrait juger en faveur du plaignant et vous pourriez perdre votre salaire, de l'argent ou vos possessions sans autre préavis.)

Vous voudrez peut-être consulter un avocat immédiatement, car la façon de procéder du tribunal peut être compliquée et les conseils d'un avocat pourraient vous être très utiles. Si vous ne connaissez pas d'avocat, vous pouvez téléphoner soit à un bureau de renseignements concernant les avocats disponibles, soit à un service d'aide juridique qui se trouvent dans l'annuaire téléphonique. Si vous n'engagez pas un avocat et décidez de prendre vous-même votre défense devant le tribunal, n'oubliez pas de mentionner sur votre réponse le numéro de votre affaire et les noms des intéressés (indiqués au haut de cette page).

L'original de votre réponse doit être soumis au greffier du tribunal à l'adresse suivante:

Clerk of the Circuit Court
Civil Division
100 E. Ocean Blvd.
Stuart, Florida 34994

P.O. Drawer 9016
Stuart, Florida 34995

Une copie de votre réponse doit également être postée ou remise à l'avocat du plaignant le nom et l'adresse qui se trouvent a coté de la marque de l'autre coté de la page.

N'oubliez pas de garder une copie de votre réponse afin de vous y référer si nécessaire.

MARTIN COUNTY CIRCUIT COURT

I. . Case Style

Plaintiff State of Florida
Public Service Commission

Case No. _____

Judge Larry Schack

VS.

Defendant Martin Downs Utilities, Inc.

II. Type of Case (Place an X in one box only. If the case fits more than one type of case -- select the most definitive.)

DOMESTIC RELATIONS - DIV. "A"	TORTS - DIV. "D"	OTHER CIVIL
_____ Simplified Dissol. (Kit)	_____ Profess. Malpractice	_____ Contracts - Div. D
_____ Dissolution	_____ Products Liability	_____ Condominium - Div. D
_____ Support - IV-D	_____ Auto Negligence	_____ Real Property - Div. C Mortg. Foreclosure
_____ Support - Non IV-D	_____ Other Negligence	_____ Eminent Domain - Div. D
_____ URESA - IV-D		_____ Const. Law - Div. - B Bond Validation
_____ ADOPTION		
_____ URESA - Non IV-D		_____ Accounting - Div. Declaratory Judgements, Specific Performance - Div - C
_____ Domestic Violence		_X_ Other - Div.
_____ Other Domestic Relations		
_____ Name Change		

II. Is Jury Trial Demanded In Complaint?

_____ Yes
_X_ No

III. Time Standard Applicable (Insert date that time standard expires)

_____

Date: August 20, 1998

SIGNATURE OF ATTORNEY FOR PARTY INITIATING ACTION:

BY: Ralph R. Jaeger

IN THE CIRCUIT COURT OF THE
NINETEENTH JUDICIAL CIRCUIT IN
AND FOR MARTIN COUNTY, FLORIDA

STATE OF FLORIDA
PUBLIC SERVICE COMMISSION

Petitioner,

vs.

MARTIN DOWNS UTILITIES, INC.

Respondent,
_____/

CASE NO.:

DIVISION:

PETITION TO ENFORCE FINAL ORDER

Petitioner, Florida Public Service Commission (Commission), by and through its undersigned attorneys and pursuant to Sections 120.69, 367.011, and 607.1406, Florida Statutes, petitions this Court to enforce Commission Order No. PSC-97-1147-FOF-WS, and in support thereof states:

BACKGROUND

1. Section 367.011(2), Florida Statutes, gives the Commission exclusive jurisdiction over each utility with respect to its authority, service, and rates.

2. Section 367.171(1), Florida Statutes, states that the provisions of that chapter shall become effective in a county of this state upon adoption of a resolution by the board of county commissioners.

3. By resolution, effective September 23, 1980, Martin County gave jurisdiction over investor-owned water and wastewater utilities in Martin County to the Commission.

4. Martin Downs Utilities, Inc. (Martin Downs or utility), an investor-owned water and wastewater utility, was incorporated in the State of Florida in April 1981. Subsequent to the above resolution, Martin Downs applied for and was granted Water Certificate No. 343-W and Wastewater Certificate No. 301-S by this Commission.

5. Initially, Martin Downs was a wholly-owned subsidiary of Southern Realty Group, Inc. (SRG). However, on January 25, 1990, Martin Downs was recapitalized and then sold by SRG, to an entity controlled by certain SRG shareholders.

6. Section 367.101, Florida Statutes, specifically gives the Commission authority over the utilities' charges for service availability. Service availability charges collected by a utility are treated as contributions-in-aid-of-construction (CIAC).

7. On October 26, 1990, Martin Downs filed for authority to continue to collect gross-up on CIAC. By Order No. 25360 (Attachment 1), issued November 19, 1991, Martin Downs was granted authority, subject to the conditions in Orders Nos. 16971 and 23541, to continue to collect the CIAC gross-up using the full gross-up formula. The collection of CIAC gross-up was designed so

that it would offset the actual income tax liability incurred by the utility for its collection of taxable CIAC.

8. Martin Downs was a Class A utility which provided services to approximately 3,486 water and 2,981 wastewater customers in Martin County. According to the 1992 annual report, operating revenues were reported as $1,112,379 for water and $1,040,717 for wastewater. The utility reported net operating income of $291,382 for the water system and $261,177 for the wastewater system.

9. In compliance with Order No. 16971, Martin Downs filed its CIAC reports for the fifteen-month period October 1, 1989 through December 31, 1990, and for the year ended December 31, 1991.

10. Martin Downs' facilities were sold to Martin County on August 12, 1993. By Order No. PSC-93-1484-FOF-WS (Attachment 2), issued October 12, 1993, in Docket No. 930818-WS, the Commission acknowledged the transfer of the water and wastewater facilities to an exempt governmental entity and canceled Certificates Nos. 343-W and 301-S.

11. The disposition of CIAC gross-up collections was not addressed by Order No. PSC-93-1484-FOF-WS. Therefore, Commission staff opened Docket No. 931065-WS on November 4, 1993 (23 days after issuance of Order No. PSC-93-1484-FOF-WS), to address the disposition of excess gross-up funds collected by Martin Downs for the period October 1, 1989 through August 12, 1993.

12. By letter dated November 23, 1993 (Attachment 3), Commission staff advised the attorney that was currently representing Martin Downs that the disposition of gross-up funds collected prior to August 12, 1993, would be addressed in the newly-opened docket. That letter referenced Orders Nos. 16971 and 23541, orders governing CIAC gross-up (orders attached as Attachments 4 and 5, respectively).

13. By that same letter, Commission staff also submitted its preliminary refund calculation numbers to the utility. This preliminary analysis indicated that the utility had collected excess gross-up, and that a refund might be required.

14. On December 16, 1993, the utility responded indicating that it disagreed with certain adjustments made by Commission staff. The Commission staff and the utility had several telephone discussions regarding the differences. As a result, by letter dated October 11, 1994, the Commission staff requested additional clarifying information.

15. However, by letter dated November 15, 1994, Martin Downs' former shareholders inquired about whether the Commission had continuing jurisdiction over the CIAC gross-up refund now that the utility was being liquidated.

16. By letter dated, November 29, 1994 (Attachment 6), counsel for the Commission advised Martin Downs that the Commission still had jurisdiction over the CIAC gross-up funds. Subsequently, on January 12, 1995, the utility responded to staff's concerns with revised schedules and additional clarifying information.

17. However, the Commission directed its staff to hold workshops to discuss the current practices employed in dealing with the taxability of CIAC and to discuss viable alternatives. While these workshops were being scheduled, the records of the Department of State show that Martin Downs was administratively dissolved as of August 25, 1995.

18. Pending the holding of these workshops, and further guidance from the Commission on the proper handling of CIAC gross-up cases, Commission staff temporarily delayed the processing of this type of case. However, by Order No. PSC-96-0686-FOF-WS, issued May 24, 1996, the Commission directed its staff to continue processing CIAC gross-up and refund cases pursuant to Orders Nos. 16971 and 23541.

19. Then, on August 20, 1996, the Small Business Job Protection Act of 1996 (The Act) became law. The Act provided for the non-taxability of CIAC collected by water and wastewater utilities effective retroactively for amounts received after June 12, 1996. Collections on or before that date remained taxable.

20. Resuming the processing of this case, Commission staff made further inquiries of Martin Downs.

21. By letter dated July 25, 1997, Steve Fry responded to these inquiries for the utility as follows:

> a. Martin Downs Utilities, Inc. (MDU) sold all of its assets to Martin County. That sale was closed in August, 1993. Subsequent to the sale, MDU was dissolved and the MDU Liquidating Trust was established to liquidate the company.
> b. The Florida Public Service Commission (PSC) relinquished its jurisdiction in October, 1993. The PSC's Order did not reserve any jurisdiction over any MDU matters.
> c. The last contact I had with the PSC was in early 1996.
> d. The Liquidating Trust was terminated in late 1996.
> e. Neither MDU nor the Liquidating Trust have any assets or employees, nor do they transact any business. There are no bank accounts.
> f. Due to two floods that occurred in the building formerly occupied by this company, and the relocation of this office, the few remaining MDU files are in a state of general disorder.
>
> Based on the foregoing, I cannot answer any of the questions described in your letter other than the first question, "Are there any funds in the CIAC Tax Impact Account of MDU?" That question is answered by . . . [e] above.

22. In reviewing the response, the Commission found that Order No. PSC-93-1484-FOF-WS, issued October 12, 1993, merely acknowledged the sale (approved as a matter of right pursuant to Section 367.071(4)(a), Florida Statutes), canceled the certificates, and closed the docket, and did not address any continuing jurisdictional questions or say anything about relinquishing jurisdiction.

23. In Proposed Agency Action (PAA) Order No. PSC-97-1147-FOF-WS (Attachment 7), issued September 30, 1997, the Commission interpreted the powers given to it by Section 367.011, Florida Statutes, and determined that it was not necessary for the October 12, 1993 Order to specifically retain jurisdiction or advise Martin Downs that refunds of CIAC gross-up for the period from October 1, 1989, through the date of sale might be required. That PAA Order was not protested and became final on October 21, 1997.

24. Also, by opening Docket No. 931065-WS (opened November 4, 1993), by sending the November 23, 1993 letter, and by several other letters and meetings, Martin Downs was given ample notice that the funds in the CIAC Tax Impact Account were still subject to refund. Further, Orders Nos. 16971 and 23541 specifically stated that the funds in this account would only be used to pay the taxes associated with the collection of the CIAC gross-up or they would be refunded to the contributors.

25. The Commission's authority to address matters which occurred prior to the cancellation of a utility's certificate has been addressed in Charlotte County v. General Development Utilities, Inc., 653 So. 2d 1081 (Fla. 1st DCA 1995). In that case, Charlotte County claimed that the utility overbilled it for service. The complaint was filed after the sale of the utility and cancellation of its certificate, but involved overbilling which occurred prior to the sale and cancellation. The Court held that

the Commission had exclusive jurisdiction over the matter which occurred before the sale and cancellation of the certificate. The Court looked to the Commission's jurisdiction as defined by Section 367.011(2), Florida Statutes, and the definition of "utility" under Section 367.021(12), Florida Statutes.

26. Through Order No. PSC-97-1147-FOF-WS, the Commission required Martin Downs to refund CIAC gross-up funds in the amount of $32,361 for the fifteen-month period ending December 31, 1990, and $22,064 for fiscal year 1991, plus accrued interest through the date of refund, for gross-up collected in excess of the tax liability for those periods. That Order further required all refund amounts to be refunded on a pro rata basis to those persons who contributed the CIAC gross-up funds within six months of the effective date of the order. Within thirty days from the date of the refund, the utility was to submit copies of canceled checks, credits applied to monthly bills or other evidence that verified that the utility had made the refunds. Within thirty days from the date of the refund, the utility was also to provide a list of unclaimed refunds detailing contributor and amount, and an explanation of the efforts made to make the refunds. No refund was required for the years 1992 and 1993.

27. The Commission has now determined that no refunds were

made and that all funds, including those in the CIAC Tax Impact Account, were dispersed by the Martin Downs Utilities Liquidating Trust (Liquidating Trust) to the shareholders several years ago. Therefore, the utility has not complied with the requirements of Order No. PSC-97-1147-FOF-WS.

ENFORCEMENT OF ORDER NO. PSC-97-1147-FOF-WS

28. Despite all indications that a refund would be required, the Liquidating Trust apparently distributed all funds without retaining at least the amount left in the CIAC Tax Impact Account to cover any possible refunds.

29. Section 607.0834(1), Florida Statutes, specifically provides in pertinent part:

> A director who votes for or assents to a distribution made in violation of s. 607.06401 . . . is personally liable to the corporation for the amount of the distribution that exceeds what could have been distributed without violating s. 607.06401 . . . if it is established that he did not perform his duties in compliance with s. 607.0830.

30. Section 607.06401(3), Florida Statutes, provides in pertinent part:

> No distribution may be made, if after giving it effect:
> (a) The corporation would not be able to pay its debts as they become due in the usual course of business;

31. In this case the Liquidating Trust apparently distributed all funds without retaining any amounts whatsoever and without giving notice to the Commission or the contributors of the CIAC gross-up to which the refund would be due. In order for a dissolved corporation to dispose of claims which are contingent, conditional, or unmatured, the corporation must, pursuant to Section 607.1406(4), Florida Statutes, give notice to the claimant. The Liquidating Trust did not appear to follow this procedure.

32. In order for a director to be held liable for an unlawful distribution, a proceeding must be "commenced within 2 years after the date on which the effect of the distribution was measured under s. 607.06401(6) or (8)." Section 607.0834(3), Florida Statutes. Although the Commission does not know when the distribution was made, the sale was not consummated until August 12, 1993, and Docket No. 931065-WS was opened on November 4, 1993. Section 607.01401(20), Florida Statutes, defines proceeding as one that "includes civil suit and criminal, administrative, and investigatory action."

33. Although there may be some question whether the opening of this docket satisfied the requirement that a proceeding be commenced within 2 years of the effect of the distribution, Section 607.1406(13), Florida Statutes, states that a shareholder may be

held liable for a claim against the corporation if a proceeding is begun prior to the expiration of three years following the effective date of dissolution. The Department of State indicates that the date of dissolution was August 25, 1995, and it appears that a proceeding against the shareholders could be brought some three years after that date.

34. In the case at hand, there was a distribution made to shareholders, and the Commission believes that both the directors who made the distribution, and the shareholders who received the distribution, could, absent certain defenses, be held liable for the refund required by Order No. PSC-97-1147-FOF-WS.

35. Section 120.69(1)(a), Florida Statutes, entitled "Enforcement of agency action," provides: "Any agency may seek enforcement of an action by filing a petition for enforcement, as provided in this section, in the circuit court where the subject matter of the enforcement is located."

36. Therefore, finding that Martin Downs has not complied with its lawful order, the Commission files this Petition to Enforce Final Order No. PSC-97-1147-FOF-WS pursuant to Sections 120.69, 367.011 and 607.1406(9)-(15), Florida Statutes. The Commission seeks to have the refund provisions of Order No. PSC-97-1147-FOF-WS enforced against either the shareholders or the directors of Martin Downs.

37. Pursuant to Section 367.011(2), Florida Statutes, the Legislature has empowered the Commission to have exclusive jurisdiction over each regulated utility with respect to the utility's authority, service and rates.

38. Section 367.011(3), Florida Statutes, states:

> The regulation of utilities is declared to be in the public interest, and this law is an exercise of the police power of the state for the protection of the public health, safety, and welfare. The provisions of this chapter shall be liberally construed for the accomplishment of this purpose.

39. The Commission's main ability to exercise the police power of the State is accomplished through enforcing compliance with its orders. *See* AMI Anclote Manor Hosp. v. State ex rel. Weber, 553 So. 2d 199, 199-200 (Fla. 2d DCA 1989) (if the legislative intent is clear that the state body has been accorded the power to protect the state's citizens, then the use of parens patriae is appropriate). Given the statutory grant of authority empowering the Commission to come before this Court to carry out its duties pursuant to Chapter 367, it would frustrate the intent of the Legislature to not enforce Commission orders.

WHEREFORE, the Petitioner, State of Florida Public Service Commission, petitions this Court to enforce Commission Final Order No. PSC-97-1147-FOF-WS, issued September 30, 1997, against either the shareholders or directors of Martin Downs Utilities, Inc.

Respectfully submitted, this 20th day of August, 1998.

ROBERT D. VANDIVER, General Counsel
Florida Bar No. 344052

Ralph R. Jaeger
RALPH R. JAEGER, Senior Attorney
Florida Bar No. 326534

FLORIDA PUBLIC SERVICE COMMISSION
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850
Telephone No.: (850) 413-6199
Facsimile No.: (850) 413-6250

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of this Petition to Enforce Final Order has been furnished by U.S. Mail, this 21st day of August, 1998, to Steve Fry, Agent for Martin Downs Utilities Liquidating Trust, Peter Cummings and Associates, 3501 Southwest Corporate Parkway, Palm City, Florida 32302-1567; and to David R. Giunta, Agent for Martin Downs Utilities, Inc., One Woodward Avenue, Suite 2400, Detroit, Michigan 48226.

Ralph R. Jaeger

Ralph R. Jaeger, Senior Attorney
FLORIDA PUBLIC SERVICE COMMISSION
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850
(850) 413-6199

ATTACHMENT 1

A Publication of FALR, Inc. P.O. Box 385, Gainesville, FL 32602 (904) 375-8836

91 FPSC 11:389

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition for authority to continue gross-up of contributions-in-aid-of-construction (CIAC) in Martin County by MARTIN DOWNS UTILITIES, INC.	DOCKET NO. 900870-WS ORDER NO. 25360 ISSUED: 11/19/91

The following Commissioners participated in the disposition of this matter:

THOMAS M. BEARD, Chairman
SUSAN F. CLARK
J. TERRY DEASON
BETTY EASLEY
MICHAEL McK. WILSON

NOTICE OF PROPOSED AGENCY ACTION
ORDER APPROVING CONTINUED GROSS-UP OF
CONTRIBUTIONS-IN-AID-OF-CONSTRUCTION

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 25-22.0290, Florida Administrative Code.

CASE BACKGROUND

In Order No. 23541, issued October 1, 1990, we determined that any water and wastewater utility currently grossing-up contributions-in-aid-of-construction (CIAC) must file a petition for continued authority to gross-up. On October 26, 1990, Martin Downs Utilities, Inc. (Martin Downs) timely filed a petition requesting approval to continue to collect the gross-up on its CIAC.

APPROVAL CONTINUE TO GROSS-UP

In accordance with Order No. 23541, Martin Downs has provided the Commission with a statement showing an actual above-the-line tax liability, cash flow statements, a statement of interest coverage indicating a times interest earned (TIE) ratio of less than 2x, and a statement that it does not have an alternative source of financing available at a reasonable rate. Further, as

justification for the gross-up, Martin Downs states that it will incur an above-the-line tax liability associated with the collection of CIAC and that it will not be able to generate the funds to finance the taxes either through its existing rates or alternative financing. Martin Downs also indicated that it selected the full gross-up method because it believes that this method is the least costly alternative and it has not resulted in competitive disadvantage or decreased growth in the service area. Finally, Martin Downs submitted proposed tariffs for the gross-up. Based on the information filed, we find that Martin Downs has demonstrated a continued need to collect the gross-up. Its request to continue collecting the gross-up is, therefore approved. The proposed tariffs filed by Martin Downs will be effective upon expiration of the protest period set forth in the Notice of Further Proceedings attached to this Order.

All CIAC gross-up collections are to be made in accordance with the accounting and regulatory treatments and record keeping prescribed in Orders Nos. 16971 and 23541, and all matters discussed in the body of those Orders are expressly incorporated herein by reference.

In consideration of the foregoing, it is

ORDERED by the Florida Public Service Commission that approval is granted for Martin Downs Utilities, Inc. to continue collecting the gross-up on CIAC. It is further

ORDERED that all gross-up CIAC collections shall be made in accordance with the provisions of Orders Nos. 16971 and 23541 which are incorporated herein by reference. It is further

ORDERED that the provisions of this Order are issued as proposed agency action and shall become final, unless an appropriate petition in the form provided by Rule 25-22.029, Florida Administrative Code, is received by the Director of the Division of Records and Reporting at his office at 101 East Gaines Street, Tallahassee, Florida 32399-0870, by the date set forth in the Notice of Further Proceedings below. It is further

ORDERED that the proposed tariffs filed by Martin Downs Utilities, Inc. shall be effective upon the expiration of the protest period set forth in the Notice of Further Proceedings attached to this Order. It is further

ORDERED that in the event no timely protest is received, this docket shall be closed.

By ORDER of the Florida Public Service Commission, this 19th day of NOVEMBER, 1991.

STEVE TRIBBLE, Director
Division of Records and Reporting

(S E A L)

NRF

ATTACHMENT 2

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Notice of Sale of Assets of Martin Downs Utilities, Inc. to Martin County, Florida.	DOCKET NO. 930818-WS ORDER NO. PSC-93-1484-FOF-WS ISSUED: October 12, 1993

ORDER ACKNOWLEDGING SALE, CANCELLING CERTIFICATES AND CLOSING DOCKET

BY THE COMMISSION:

On August 17, 1993, Martin Downs Utilities, Inc. (Martin Downs or Utility) filed an application with this Commission for acknowledgment of the transfer of its water and wastewater facilities to Martin County. The sale occurred on August 12, 1993.

The provisions of Section 367.071, Florida Statutes, require an application for approval of sale or transfer of water and/or wastewater utilities to governmental agencies, although such sales are approved as a matter of right. Subsection 367.022(2), Florida Statutes, exempts from regulation by the Commission systems owned, operated, managed or controlled by governmental agencies.

Rule 25-30.037(3)(e), Florida Administrative Code, requires a utility to submit a statement regarding disposition of customer deposits. All customer deposits held by Martin Downs were transferred to Martin County upon consummation of the sale. Commission requirements regarding regulatory assessment fees have been met, and there are no dockets pending involving this system.

On the basis of the foregoing, we find it appropriate to acknowledge the transfer of the water and wastewater facilities of Martin Downs to Martin County and cancel Certificates Nos. 343-W and 301-S. The Certificates have been returned to this Commission for cancellation. It is, therefore,

ORDERED by the Florida Public Service Commission that the sale of the facilities of Martin Downs Utilities, Inc., Post Office Box 620, Palm City, Florida 34990, to Martin County Board of County Commissioners, 2401 Southeast Monterey Road, Stuart, Florida 33496, is hereby acknowledged. It is further

ORDERED that Certificates Nos. 343-W and 301-S are hereby cancelled. It is further

ORDERED that Docket No. 930818-WS is hereby closed.

By ORDER of the Florida Public Service Commission this 12th day of October, 1993.

STEVE TRIBBLE, Director
Division of Records and Reporting

(S E A L)

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), 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.

Any party adversely affected by the Commission's final action in this matter may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of Records and Reporting within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or sewer 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 after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Civil Procedure. The notice of appeal must be in the form specified in Rule 9.900 (a), Florida Rules of Appellate Procedure.

State of Florida ATTACHMENT 3

DIVISION OF WATER &
WASTEWATER
CHARLES HILL
DIRECTOR
(904) 488-8482

Public Service Commission

November 23, 1993

Mr. F. Marshall Deterding
Rose, Sundstrom & Bentley
Post Office Box 1567
Tallahassee, Florida 32302-1567

Dear Mr. Deterding:

According to our records, the purchase of Martin Downs Utilities, Inc.'s facilities was concluded on August 12, 1993. By Order No. PSC-93-1484-FOF-WS, in Docket No. 930818-WS, issued October 12, 1993 the Commission acknowledged transfer of the system. The disposition of CIAC gross-up funds was not addressed in that docket. However, Order Nos. 16971 and 23541 require that any gross-up amounts collected in excess of a utility's actual tax liability resulting from its collection of CIAC, shall be refunded on a pro rata basis to the contributors of those amounts. Therefore, we are required to address the disposition of gross-up funds even though the utility's facilities have been sold to the County.

Staff must address the collection of gross-up funds from October 1, 1989 through August 12, 1993. We are in receipt of the gross-up information for the years ending 1990 and 1991. Order Nos. 16971 and 24129 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 and whether a refund of the gross-up is appropriate for any given year for which gross-up was in effect. If the utility was not grossing-up during any period, please provide a statement from the previous owners that would confirm that gross-up was not collected. Before we can finalize our calculations, the following CIAC gross-up information must be provided for each year for the period January 1, 1992 through December 31, 1992 and the period January 1, 1993 through August 12, 1993.

1. A detailed statement of the CIAC tax impact account;

2. Signed copies of the utility's federal and state income tax returns or completed copies of the CIAC report form (copy attached), (Federal and State tax returns filed in connection with CIAC gross-up may be given confidential treatment if filed in accordance with Rule 25-22.006, Florida Administrative Code.

3. Workpapers which show the treatment of CIAC on the tax return.

In addition to the above three items, staff requests the following:

1. The actual above-the-line tax liability before the effect of CIAC is taken into consideration;

2. The actual above-the-line tax liability after the effect of CIAC is taken into consideration;

3. The amount of CIAC collected for the reporting period;

4. The amount of gross-up collected for the reporting period;

5. Calculation of the amount of over or under collection of CIAC gross-up;

6. The proposed amount of refund and interest, if any;

7. The proposed method of refund.

We have reviewed the CIAC gross-up reports as filed for each year 1990 through 1991. Based on our review of the files, staff believes the utility has collected gross-up in excess of the amount of taxes related to the collection of taxable CIAC. A copy of our preliminary analysis of the refund calculation is attached. This calculation is consistent with the calculation adopted by the Commission in Order No. PSC-92-0961-FOF-WS. If you disagree with our preliminary calculation, please provide us with supporting documentation.

In addition, our review of the 1990 and 1991 CIAC gross-up reports resulted in several questions. We are unable to determine how the above-the-line income and below-the-line income relates to the taxable income reported on your tax return. Please provide a reconciliation for the taxable income as reported on the 1990 and 1991 Income Tax Returns with the taxable income reflected in exhibits no. 1 of CIAC gross-up reports. Until data addressing these questions have been received, our calculations cannot be finalized.

Company response to the above questions should be provided no later than December 23, 1993. Gross-up refunds and verification of the refunds will be required and monitored regardless of whether the certificate has been cancelled due to the sale to Martin County.

Should you have any questions, please let me know.

Sincerely,

Jennifer J. Iwenjiora
Regulatory Analyst

/jji
Enc. (2)
cc: Division of Water and Wastewater (Hill, Kosloski, Meador)
Division of Legal Services (O' Sullivan, Summerlin)
Division of Auditing & Financial Analysis (Hicks)
Mr. Jonathan Ferguson, County Attorney

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Request by FLORIDA WATERWORKS ASSOCIATION for investigation of proposed repeal of Section 118(b), Internal Revenue Code (Contributions in Aid of Construction).	DOCKET NO. 860184-PU ORDER NO. 16971 ISSUED: 12-18-86

The following Commissioners participated in the disposition of this matter:

GERALD L. GUNTER
JOHN T. HERNDON
KATIE NICHOLS
MICHAEL McK. WILSON

NOTICE OF PROPOSED AGENCY ACTION

ORDER GRANTING FLORIDA WATERWORKS ASSOCIATION'S "APPLICATION FOR EMERGENCY APPROVAL OF AMENDED SERVICE AVAILABILITY POLICIES" WITH MODIFICATIONS

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service Commission of its intent to grant, pursuant to Sections 367.011, 367.0823, 367.101, and 367.121, Florida Statutes, and Rule 25-30.508, Florida Administrative Code, approval of the Florida Waterworks Association's request that water and sewer utilities subject to this Commission's jurisdiction be allowed to amend their service availability policies to meet the tax impact on Contributions in Aid of Construction (CIAC) resulting from the amendment of Section 118(b) of the Internal Revenue Code.

BACKGROUND

Congress has passed and the President has signed the Tax Reform Act of 1986 (Act), which amends, effective January 1, 1987, Section 118(b) of the Internal Revenue Code.

Section 118 is entitled, "Contributions to the capital of a corporation". Section 118(a) states, "In the case of a corporation, gross income does not include any contribution to the capital of the taxpayer." Prior to the passage of the Act, Section 118(b)(1), entitled "Contributions in aid of construction", stated,

> Contributions in aid of Construction. (1) General Rule. For purposes of this section, the term "contribution to the capital of the taxpayer" includes any amount of money or other property received from any person (whether or not a shareholder) by a regulated public utility which provides electric energy, gas (through a local distribution system or transportation by pipeline), water, or sewerage disposal services if--
>
> (A) such amount is a contribution in aid of construction,

(B) where the contribution is in property which is other than electric energy, gas, steam, water, or sewage disposal facilities, such amount meets the requirements of the expenditure rule of paragraph (2), and

(C) such amounts (or any property acquired or constructed with such amounts) are not included in the taxpayer's rate base for rate-making purposes.

Section 118(b) now reads:

(b) CONTRIBUTIONS IN AID OF CONSTRUCTION ETC.--For purposes of subsection (a), the term "contribution to the capital of the taxpayer" does not include any contribution in aid of construction or any other contribution as a customer or potential customer. (Emphasis supplied).

Thus CIAC paid to a utility by developers and other customers may be treated as gross income to the utility and may be subject to taxation.

REQUEST OF FLORIDA WATERWORKS ASSOCIATION

In response to the change in the tax law, the Florida Waterworks Association has requested that this Commission enter an order which provides as follows:

a) On and after January 1, 1987, the effective date of the repeal of Section 118(b) of the Internal Revenue Code, utilities may collect from developers and others who transfer property and amounts to a utility as CIAC, which transfers had been excluded from taxable income pursuant to Section 118(b) of the Internal Revenue Code an amount equal to the tax impact.

b) The tax impact amount to be collected shall be determined using the formula

$$\text{TAX IMPACT} = \frac{R}{1.0-R} \times (F + P)$$

1) R = Applicable marginal rate of Federal and State Corporate Income Tax if one is payable on the value of contributions which must be included in taxable income of the utility.

2) R shall be determined as follows:

R = ST + FT (1-ST)

ST = Applicable marginal rate of State Corporate Income Tax

FT = Applicable marginal rate of Federal Income Tax, either corporate or individual.

3) F = Dollar Amount of charges paid to a utility as contributions in aid of construction which must be included in taxable income of the utility, and which had been excluded in taxable income pursuant to Section 118(b) of the Internal Revenue Code.

4) P = Dollar amount of property conveyed to utility which must be included in taxable income of the utility, and which had been excluded from taxable income pursuant to Section 118(b) of the Internal Revenue Code.

c) The CIAC tax impact amounts, as determined in Paragraph (b), shall be deposited as received into a fully funded interest bearing escrow account, hereinafter referred to as the "CIAC Tax Impact Account". Monies in the CIAC Tax Impact Account may be withdrawn periodically for the purpose of paying that portion of the estimated Federal and State income tax expense which can be shown to be directly attributable to the repeal of Section 118(b) of the Internal Revenue Code and the inclusion of CIAC in taxable income. Annually, following the preparation and filing of the utility's annual Federal and State income tax returns, a determination shall be made as to the actual Federal and State income tax expense that is directly attributable to the inclusion of CIAC in taxable income for the tax year. CIAC tax impact monies received during the tax year that are in excess of the actual amount of tax expense that is attributable to the receipt of CIAC, together with interest earned on such excess monies held in the CIAC Tax Impact Account must be refunded on a pro rata basis to the parties which made the contribution and paid the tax impact amounts during the tax year. The utility is required to maintain adequate records to account for the receipt, deposit, and withdrawal of monies in the CIAC Tax Impact escrow account. A detailed statement of the CIAC Tax Impact Account, including the annual determination of actual tax expense attributable to the repeal of Section 118(b) of the Internal Revenue Code shall be submitted as a part of the utility's annual report.

d) The amount of CIAC Tax Impact collected by a utility shall not be treated as CIAC for ratemaking purposes.

We shall grant Florida Waterworks Association's request subject to the following modifications:

1. All net savings in tax expense resulting from passage of the Act related to jurisdictional operations shall be offset against any increases in tax expense due to taxation of CIAC before monies are withdrawn from the escrow account.

2. Annually, following the preparation and filing of the utility's annual Federal and State income tax returns, the utility shall file with the Commission the following information which will receive confidential treatment:

a. Signed copies of said Federal and State Income tax returns.

b. Workpapers, related to said returns, which show the treatment of CIAC on said returns.

c. Workpapers showing the calculation of any tax savings resulting from the Act and related to jurisdictional operations.

3. In the event that excess monies are determined to have been withdrawn from the escrow account, the utility shall repay said monies to the account together with any earnings on the account lost because of the withdrawal.

4. The report of the escrow account activity shall include a record of interest earned and refunded as well as a calculation of tax savings.

In the event that a utility does not wish to furnish its tax return, a substitute reporting format acceptable to staff may be provided with assurance that signed copies of the tax return are available to staff upon request for review and audit.

REQUEST FOR LETTER RULING
FROM INTERNAL REVENUE SERVICE

It is possible to interpret the language of the amended Section 118(b) in such a manner that CIAC received from developers and CIAC received from future ratepayers can be segregated so that only CIAC receipts from future ratepayers would be subject to taxation. As there would appear to be some support for this position in prior litigation in the area, this idea is worth pursuing. Also, some items of taxation may be avoided if title does not pass. This possibility should also be pursued.

Consequently, we will require the Florida Waterworks Association to have one of its members request from the Internal Revenue Service a letter ruling to clarify the meaning of the new Section 118(b).

This Commission shall participate fully in the letter ruling process. This includes the drafting and approval of the request and all subsequent meetings on the issue with the Internal Revenue Service. All contacts with the Internal Revenue Service by any party shall be reported.

In view of the emergency nature of this matter, the time period for protesting this PAA order shall expire on December 31, 1986.

In consideration of the above, it is

ORDERED by the Florida Public Service Commission that the request of the Florida Waterworks Association, as set forth and modified in the body of this order, is granted. It is further

ORDERED that the Florida Waterworks Association shall, within a reasonable time, have one of its members request from the Internal Revenue Service a letter ruling clarifying the meaning of the new Section 118(b) of the Internal Revenue Code, with respect to the matters raised herein. It is further

ORDERED that this Commission shall fully participate in the letter ruling process. It is further

ORDERED that this Docket shall remain open to handle any generic problems that arise in accounting for CIAC (including gas and electric CIAC) and the related tax expenses. It is further

ORDERED that the provisions of this order, issued as proposed agency action, shall become final unless an appropriate petition in the form provided by Rule 25-22.036, Florida Administrative Code, is received by the Director of

Records and Reporting at his office at 101 East Gaines Street, Tallahassee, Florida 32399-0870, by the close of business on December 31, 1986.

By ORDER of the Florida Public Service Commission, this 18th day of DECEMBER, 1986.

STEVE TRIBBLE, Director
Division of Records and Reporting

(S E A L)

MJB

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes (1985), to notify parties of any administrative hearing or judicial review of Commission orders that may be available, as well as the procedures and time limits that apply to such further proceedings. This notice should not be construed as an endorsement by the Florida Public Service Commission of any request nor should it be construed as an indication that such request will be granted.

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 at his office at 101 East Gaines Street, Tallahassee, Florida 32399-0870, by the close of business on December 31, 1986. In the absence of such a petition, this order shall become effective January 1, 1987, as provided by Rule 25-22.029(6), Florida Administrative Code, and as reflected in a subsequent order.

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 January 1, 1987, any party adversely affected may request judicial review by the Florida Supreme Court by the filing of a notice of appeal with the Director, Division of Records and Reporting and the filing of a copy of the notice and filing fee with the Supreme Court. This filing must be completed within 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.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Request by FLORIDA WATERWORKS ASSOCIATION for investigation of proposed repeal of Section 118(b), Internal Revenue Code [Contributions-in-aid-of-construction]	DOCKET NO. 860184-PU ORDER NO. 23541 ISSUED: 10-1-90

The following Commissioners participated in the disposition of this matter:

MICHAEL McK. WILSON, Chairman
BETTY EASLEY
GERALD L. GUNTER

APPEARANCES:

B. KENNETH GATLIN, Esquire, Gatlin, Woods, Carlson & Cowdery, 1709-D Mahan Drive, Tallahassee, Florida 32308
On behalf of the Florida Waterworks Association

ROBERT M. C. ROSE, Esquire, Rose, Sundstrom & Bentley, 2548 Blair Stone Pines Drive, Tallahassee, Florida 32301
On behalf of Aloha Utilities, Inc., Canal Utilities, Inc., Clay Utility Company, Eagle Ridge Utilities, Inc., El Agua Corporation, and Martin Downs Utilities, Inc.

F. MARSHALL DETERDING, Esquire, Rose, Sunstrom & Bentley, 2548 Blair Stone Pines Drive, Tallahassee, Florida 32301
On Behalf of Alafaya Utilities, Inc., Aloha Utilities, Inc., Canal Utilities, Inc., Clay Utility Company, Eagle Ridge Utilities, Inc., El Agua Corporation, Kingsley Service Company, Lehigh Utilities, Inc., Martin Downs Utilities, Inc., Neighborhood Utilities, Inc., North Fort Myers Utility, Inc., Rolling Oaks Utilities, Inc, Royal Utility Company, and Southside Utilities, Inc.

PATRICK K. WIGGINS, Esquire, Wiggins & Villacorta, P. A., 501 East Tennessee Street, P. O. Drawer 1657, Tallahassee, Florida 32302
On behalf of Southwest Florida Capital Corporation and the Florida Home Builders Association

ROBERT J. PIERSON, Esquire, Florida Public Service Commission, 101 East Gaines Street, Tallahassee, Florida 32399-0863
On behalf of the Commission Staff

PRENTICE P. PRUITT, Esquire, Florida Public Service Commission, 101 East Gaines Street, Tallahassee, Florida 32399-0862
Counsel to the Commission

ORDER AUTHORIZING CONTINUED USE OF THE GROSS-UP OF CONTRIBUTIONS-IN-AID-OF-CONSTRUCTION, SUBJECT TO PRIOR COMMISSION APPROVAL, PRESCRIBING ACCOUNTING AND REGULATORY TREATMENTS FOR THE GROSS-UP, AND REQUIRING REFUNDS OF CERTAIN GROSS-UP AMOUNTS COLLECTED

BY THE COMMISSION:

CASE BACKGROUND

On February 13, 1986, the Florida Waterworks Association (FWWA) requested that we investigate a proposed repeal of Section 118(b), Internal Revenue Code (I.R.C.), under which certain contributions to the capital of a corporation were excludable from gross income. Ultimately, Section 118(b), I.R.C., was repealed by the Tax Reform Act of 1986 (ACT) and, effective January 1, 1987, contributions-in-aid-of-construction (CIAC) became both gross income and depreciable for federal tax purposes.

By Order No. 16971, issued December 18, 1986, on an emergency basis, this Commission authorized corporate utilities subject to our jurisdiction to amend their service availability policies to gross-up CIAC in order to meet the tax impact resulting from the inclusion of CIAC as gross income. Since then, 44 water and/or wastewater utilities have elected to implement that gross-up. Of these, only 37 remain subject to our jurisdiction.

By Order No. 21266, issued May 22, 1989, this Commission proposed to establish certain guidelines to control the collection

of the gross-up. On June 12, 1989, Order No. 21266 was protested by FWWA and 14 water/wastewater utilities.

On June 13, 1989, South Florida Capital Corporation (SFCC), under the misnomer of Florida Home Development Corporation, purported to file a petition protest to Order No. 21266. The protest was, however, untimely; accordingly, we treated it as a petition to intervene and granted SFCC intervenor status by Order No. 21921, issued September 19, 1989. On April 5, 1990, the Florida Home Builders Association (FHBA) petitioned to intervene in this proceeding. Its petition was granted by Order No. 22859, issued April 26, 1990.

By Order No. 21436, issued June 26, 1989, we also proposed to require a number of utilities to refund amounts of the gross-up collected or make adjustments to their depreciation reserves. On or about July 17, 1989, Order No. 21436 was protested by six water/wastewater utilities.

Based upon the protests of Orders Nos. 21266 and 21436, we conducted a hearing on April 27, 1990. We were not able to complete all of the testimony on that date, however, and the hearing was, accordingly, continued on April 30, 1990.

FINDINGS OF FACT, LAW, AND POLICY

Having heard the evidence presented at hearing, and having reviewed the briefs of the parties and the recommendations of Staff, we enter our findings of fact, law, and policy as follows.

RETENTION OF GROSS-UP

Purpose of Gross-up

Some of the Petitioners expressed concern that there is language in Order No. 21266 that implies that Order No. 16971, which originally authorized the gross-up, was issued solely for the purpose of alleviating cash flow problems. Although Order No. 21266 has been protested and is, therefore, a legal nullity, we note that neither FWWA's original petition nor Order No. 16971 specifically mention cash flow as a consideration. Order No. 16971 merely discusses the change in Section 118(b), I.R.C., FWWA's proposal, and our modifications to its proposal. It does not state that the gross-up was allowed solely for the purpose of alleviating

cash flow problems nor, for that matter, any other reason. Although we believe that cash flow is a consideration in the overall gross-up picture, it is only one of many.

Avoidance of Taxes on CIAC

The first question that should be addressed is whether there is any way for utilities to avoid taxes on CIAC. The IRS issued Notice 87-82 to provide guidance to taxpayers regarding the application of the tax accounting rules related to CIAC. Notice 87-82 states, in part, that "a transaction will be treated as CIAC if such treatment is in accordance with the substance of the transaction, regardless of the form in which such transaction is conducted".

Witness Elliott testified that, since the IRS generally considers any contribution of funds received by a utility related to its future provision of service to be CIAC, it is clear that if the transaction is CIAC in substance, it will be treated as CIAC for tax purposes. Witnesses Elliott and Martin also testified that they and other experts in the areas of taxation, utility law, and accounting had made diligent searches to determine whether there are any methods of avoidance of taxation on CIAC. Witness Martin's conclusion was that the Tax Reform Act of 1986 closed all loopholes to exempt CIAC from taxable income and that only new legislation from Congress could alter that position. Witness Elliott testified that he was not aware of any methods of avoiding the taxation of CIAC. However, he did not preclude the possibility of such a method.

Witness Causseaux testified that General Development Utilities, Inc. (GDU) had managed to avoid taxes on CIAC. However, she admitted that GDU's method was quite complicated, and that it probably would not be within the reach of those utilities that are most in need of the gross-up.

Although GDU's plan probably would not be within the reach of those utilities who would be most in need of the gross-up, it does indicate that there are ways to avoid taxes on CIAC. Accordingly, we hereby encourage the water and wastewater industry to continue to search for viable methods.

Who Should Bear the Burden?

If the taxation of CIAC is not generally avoidable, the next question is who should be responsible for the taxes? In their brief, SFCC and FHBA argue that the utility (i.e., the general body of ratepayers) should be responsible for paying the taxes irrespective of the source of income. They argue that to do otherwise would misidentify the contributor as the cost causer.

Witnesses Elliott and Nixon believe that the contributor is the cost causer. However, under cross-examination, Mr. Elliott agreed that measuring the extent to which any contributor is the cost causer is a very subjective determination. Mr. Elliott further stated that the decision whether to collect the taxes from the contributor should be up to each utility, based upon its particular facts and circumstances.

Witness Nixon testified that, if utilities do not gross-up, their payment of taxes on CIAC will, eventually, result in increased revenue requirements. Witnesses Martin, Elliott and Causseaux agreed. Witnesses Martin and Nixon testified that the required revenue increases may be significant, especially in high growth areas. Mr. Nixon also testified that utilities making regular and significant investments in taxes on CIAC may require regular and significant rate relief. He also argued that, due to "regulatory lag", a utility may never be able to actually earn its authorized rate of return.

Under cross-examination, however, Witness Nixon admitted that, depending upon a utility's particular circumstances, its investment in taxes on CIAC could result in either no increase or a very minimal increase in rates. Witness Causseaux also testified that a utility with prior tax losses may use them to offset current taxable income. It might, therefore, not feel the impact of the tax on CIAC for years.

We agree that high growth could result in increased revenue requirements. However, such growth would probably cause the utility to file a rate increase anyway, due to factors such as increased rate base and operating and maintenance expenses. Accordingly, we do not believe that this particular piece of the regulatory puzzle should be viewed in isolation. We believe that all of the facts and circumstances of the utility should go into determining who should bear the responsibility of paying the tax

impact of CIAC. Depending upon its particular facts and circumstances, it may be appropriate for the utility to collect the taxes from the contributor or invest in them itself.

Debt Financing for CIAC Taxes

If a utility pays the taxes associated with CIAC itself, it must obtain the cash to pay those taxes. Witnesses Martin, Nixon, and O'Steen testified that it would be difficult to obtain debt financing for the tax liability associated with the receipt of CIAC. Witness O'Steen argued that it is not a sound practice to finance a tax paid annually over a longer period of time. In fact, he argued that it may not even be possible due to the inability to collateralize such loans and the fact that the period during which the utility would recover the taxes through depreciation would be much longer than the term of the loan.

Witness O'Steen also testified that, over the long-run, investing in taxes can "damage the soundness of a utility's capital structure, thereby making it much more difficult for a utility to obtain needed funds for plant construction, renovation, and major maintenance when those funds are needed." He believes that, as utilities borrow more and more to pay such taxes, they will appear more risky to lenders, which will further restrict the availability of funds, and make those funds that are available more costly. Upon cross-examination, however, Witness O'Steen agreed that lenders place great reliance on cash flow projections.

Witness Nixon testified that most of the companies he deals with generally provide for plant expansion through debt. He argued that anything that would decrease a utility's ability to borrow funds jeopardizes its ability to serve its customers.

Witness Martin argued that the water and wastewater industry is already highly leveraged, and he expressed concern over these utilities increasing their levels of debt. He was also concerned whether funds would be available with reasonable terms and cost rates for the payment of taxes or for other purposes. He expressed particular concern about utilities that are experiencing significant growth and would have to make substantial investment in taxes every year. On cross-examination, however, Witness Martin agreed that a well-managed utility should be able to foresee and plan for such growth and increased taxes. He also agreed that a utility can petition for increased rates to improve its debt

service capability or for the gross-up if it foresees substantial growth coming.

Finally, we note that utilities do not always borrow funds for specific purposes. For instance, a company can often secure a line of credit by merely demonstrating a cash flow and paying a small fee or percentage at the front end. These funds can be used to finance anything from plant expansion to operating expenses, including the payment of taxes.

Based upon the evidence of record and the discussion above, we find that debt financing may be available for the payment of taxes related to CIAC. However, we also find that a utility's payment of taxes on CIAC may lessen its cash flow, which may, in turn, impair its ability to borrow funds for the payment of taxes or for other purposes.

Use of Cash CIAC to Pay Taxes

In her testimony, Witness Causseaux suggested that a utility in a strong cash position could use a portion of the cash CIAC to pay the taxes associated with the receipt of CIAC. However, she also stated that using cash CIAC for such a purpose will mean that there is less cash available for current or future construction or to repay the utility for its past investment in plant.

Witness Nixon testified that it would be imprudent for most utilities to use cash CIAC to meet their tax liabilities. He also stated that it defeats the very purpose for collecting CIAC, under general regulatory theory, because CIAC is primarily a financing vehicle used to construct new plant or repay debt or equity invested to construct plant. In his opinion, it should be used only for the above-mentioned purposes since CIAC must be deducted from rate base, which reduces the return available for funding debt or equity costs.

Witness Nixon also testified that many utilities' loan agreements require them to assign or pledge cash CIAC to service debt and, for that reason, cash CIAC is unavailable to meet the tax liability. Witness Deterding expressed many of the same concerns in his testimony.

Based upon the evidence of record, we find that a utility can use cash CIAC for any purpose that it deems appropriate. However,

this may mean that the cash will not be available for its intended use. Further, in a rate proceeding, all CIAC will be considered in the reduction of the utility's rate base.

Cash Versus Property CIAC

In Order No. 21266, we made the assertion that property CIAC was typically collected from developers, while cash CIAC was typically collected from individuals. In his testimony, Witness Nixon stated that cash CIAC is generally paid by developers and homebuilders. He stated that cash CIAC is less often collected directly from individual homebuyers.

Mr. Nixon also prepared an exhibit to demonstrate that the donation of cash CIAC varies between utilities. According to Mr. Nixon's exhibit, during 1987, Rolling Oaks Utilities, Inc. received $327,324 in cash contributions from individual homeowners and no cash from developers. Clay Utility Company, on the other hand, received no cash from individual homeowners and $886,745 in cash from developers. This same situation can be observed between other utilities during 1988.

In her testimony, Witness Causseaux stated that she had no knowledge of any utilities that typically collected cash CIAC from individuals as opposed to developers.

Based upon the evidence of record, we find that a utility's collection of CIAC can vary between cash and property depending upon that utility's particular facts and circumstances.

Gross-up cause Competitive Disadvantage?

This issue addresses whether implementing the gross-up of CIAC may place a utility at a competitive disadvantage with utilities that do not gross-up, or convince developers to utilize septic tanks instead of connecting to the utility's system. During the hearing, Jacksonville Suburban Utility Corporation was the only company specifically mentioned that chose not to gross-up because of competitive pressures.

Witness Nixon testified that he was not aware of any case in which a utility had chosen to gross-up but was later forced to stop due to competitive pressures. However, during cross examination,

he did admit that competition was one reason that he did not urge a mandatory gross-up.

Witness Elliott, on the other hand, testified that the water and wastewater industry in Florida is subject to competitive pressures due to the large number of both municipal and investor-owned water and wastewater utilities. He also stated that a significant difference in rates or CIAC charges can cause growth to shift into a lower-cost utility's service areas.

As for the suggestion that the gross-up may force developers to begin utilizing septic tanks, Witness Causseaux stated that she had no personal knowledge of any utilities that have had a developer switch to use of septic tanks because of gross-up costs. Although SFCC and FHBA stated that they have actual knowledge of projects utilizing septic tanks because of the CIAC gross-up cost, their position is not supported by the record. Further, Witness Nixon provided the results of a questionnaire sent to all utilities utilizing the gross-up. All of the utilities that responded stated that they were not aware of any cases in which septic tanks had been utilized or utilities had found themselves at a competitive disadvantage because of the gross-up.

Based on the evidence discussed above, we find that, although the use of the gross-up may place a utility at a competitive disadvantage, it is not a widespread problem in Florida.

Retention of Gross-up/Requirement of Pre-approval

All parties and the Staff of this Commission (Staff) agreed that the gross-up should be retained. The only real point of contention appears to be whether the gross-up should be allowed solely at the discretion of the utilities or only upon the prior approval of this Commission. All of the utility witnesses believe that whether to gross-up should be a management decision. According to witness Elliott, "management has the experience and knowledge of the facts and circumstances of the utility..." and is, therefore, in the best position to determine the needs of the utility."

We do not agree. Generally, we do not insert ourselves into the day-to-day decision-making processes of a utility. In fact, we normally do not review the management decisions of a utility unless it has applied for a rate increase or we have initiated an

overearnings investigation. In the case of the gross-up, however, the dollar amounts are quite large and there are other persons involved, such as developers and home purchasers. If we wait until a utility's next rate proceeding to review its decision whether to gross-up, it may be too late to undo what has already been done.

In addition to the above, we believe that requiring pre-approval of the gross-up is reasonable for a number of other reasons. First, out of the approximately 700 water and wastewater utilities regulated by this Commission, only 44 have ever requested to gross-up. Although a number of the utilities that we regulate are partnerships and sole proprietorships, the fact that so few have elected to implement the gross-up indicates that the vast majority of water and wastewater utilities do not need the gross-up.

The evidence also indicates that some of the utilities that are collecting the gross-up may not actually need it. For instance, Witness Nixon stated that one company, Southern States Utilities, Inc., appears to have enough resources to cover the tax impact of CIAC, and that it intends to discontinue the gross-up. Witness Nixon stated that Florida Cities Water Company is another company that "will not fight for continued authority to gross-up."

Second, the use of a gross-up creates a new tax, and expense, that did not previously exist. This is what has been referred to as the "tax-on-tax." A tax-on-tax is created when taxes are contributed. The contributed taxes are considered gross income which are, in turn, taxable. Because of this tax-on-tax effect, the gross-up can be as high as 60.3 percent, as compared to a maximum combined federal and state tax rate of 37.63 percent, if the utility pays the tax on CIAC itself.

Witness Elliott stated that this "tax-on-tax" effect does not only exist in the case of a gross-up. He stated that, when a utility does not gross-up, it must use equity to invest in the CIAC-related taxes. Since the equity component is grossed-up for taxes, he argues that there is a "tax-on-tax." Although a portion of the CIAC tax investment would be supported by equity, we do not believe that Witness Elliott's analysis considers that we generally do pro rata reconciliations, assuming that funds cannot be traced. Witness Elliott's analysis also assumes that equity would be the only source available for financing. Although funds cannot be specifically traced, we believe that there are other sources for

these funds, such as operating revenues, debt, and deferred taxes.

Witness Causseaux argued that the tax on CIAC is a cost of doing business. Witness Elliott agreed. He also stated his belief that "the change in the tax laws have imposed a new cost on the utilities associated with CIAC." An observation was also made at the hearing that, if Congress had wanted to tax the contributor, it would have done so. Over the long-run, however, it is probably the homeowner/ratepayer who bears the burden anyway.

Upon consideration of the above, we believe that the gross-up should be retained, but that it should only be allowed upon the prior approval of this Commission.

Determination of Need

We believe that the need for a gross-up should be determined on a case-by-case basis, based upon the facts and circumstances peculiar to each utility. According to Witness Elliott, utility management is in the best position to evaluate all of these facts and circumstances, and to determine whether a gross-up is needed and, if so, what methodology to use. If that is the case, once management determines that a gross-up is necessary, it should be able to provide the same information that it relied upon to make such a determination in a petition to this Commission. Accordingly, we find it appropriate to require all utilities that wish to collect the gross-up to file a petition for approval to collect the gross-up with this Commission. Any utility that is already collecting the gross-up may continue to do so pending our approval of its petition, provided that it files such a petition on or before October 29, 1990.

There is, of course, no need determination policy that will cover the entire water and wastewater industry. Our requirements must, therefore, remain flexible. However, at a minimum, each utility [illegible] to demonstrate that a tax liability exists and that [illegible] are not available at a reasonable cost. Generally speaking, a utility may demonstrate such need by filing the following information:

Demonstration of Actual Tax Liability - As a threshold, a [illegible] demonstrate the existence of an actual [illegible] above-the-line basis. Unless there

[redacted] tax liability, there is no need for additional [redacted]

Cash Flow Statement - All Class A and B utilities ought to be able to provide a cash flow statement. Witness O'Steen stated that a prudent utility would have cash flow statements for a number of years. He also stated that in his experience as a banker he "zeroed in on the cash flow." A cash flow statement would show whether liquid funds are available to pay taxes on CIAC. We will not require cash flow statements from Class C utilities, however, due to the expense associated with them.

Statement of Interest Coverage - The utility should also provide a statement of its times interest earned (TIE) ratio. The TIE ratio indicates the number of times a utility is able to cover its interest. The ratio is an indicator of the relative protection of the bondholders. It is also indicative of a utility's ability to go into the financial market to borrow money or issue stock at a reasonable rate. A utility should demonstrate that its TIE ratio is no more than 2x. We have selected a TIE ratio of 2x because the testimony indicates that it is a conservative ratio that maintains a utility's financial integrity without unduly burdening the ratepayers. We also note that 2x is within the range of Moody's Baa guidelines. Witness Elliott testified that 2x was too low; however, he did not present an alternative. Although we believe that a TIE ratio of 2x should be used as a benchmark, it should not be viewed in isolation. A utility may be able to show adequate interest coverage, but not have enough cash on hand.

Statement of Alternative Financing - A utility should also be able to demonstrate that it does not have an alternative source of financing available at a reasonable rate. As discussed above, some utilities may not be able to obtain financing at a reasonable rate to pay for taxes on CIAC. However, certain situations may exist where an alternative source is available at a reasonable rate. For instance, under cross-examination, Witness Elliott admitted that, given the choice between giving or lending the funds to pay taxes on CIAC, there was a strong incentive for a contributor to lend them.

Justification for Gross-up - The utility should also provide a statement regarding why it needs the gross-up, including the particular facts and circumstances that led to that conclusion. As stated by Witness Causseaux, "the utility is intimately aware of

its own unique circumstances ... [and] should be able to articulate its reasons for requesting a gross-up."

Gross-up Method Selected - The utility should also indicate the gross-up method selected and the reasons why. As discussed below, there are two methods of calculating the gross-up, each with its own advantages and disadvantages. Since the utility knows its unique circumstances leading to the decision to request the gross-up, it should also determine which gross-up method is better in its situation.

Proposed Tariffs - Finally, the utility should submit proposed tariffs for the gross-up in its filing.

Frequency of Demonstration of Need

One of the concerns of the utilities is whether the gross-up need determination will be one-time or periodic. In his testimony, Witness Nixon argued that an annual review of the need for the gross-up could cost anywhere between $5,000 to $8,000 a year for accounting services alone. He believes that it would be an unwarranted additional expense to pass on to the ratepayers. Mr. Nixon also stated that any fluctuations in need from year to year could result in discriminatory rates being applied to new connections. Upon cross-examination, however, he agreed that, once a utility has an approved gross-up, it should be simple for it to advise this Commission on an annual basis whether its circumstances had changed.

Witness Martin also argued that an annual determination of need would be expensive. He also testified that it will be difficult for utilities to forecast their cash flow for ten or 15 years if they face the prospect of losing the gross-up each and every year. Mr. Martin stated that this "unstabilizing event" could be looked upon unfavorably by lenders, bond buyers, or bond rating agencies. He also argued that a change in the gross-up for any future year could cause changes in the utility's debt service coverage and could harm the utility's ability to obtain low-cost, long-term financing.

Witness Elliott testified that it would be appropriate for us to require utilities to file a periodic statement whether any circumstances surrounding their need for the gross-up have changed. He believes that utilities should periodically review their needs

anyway, particularly if the facts and circumstances attending their decision to request the gross-up have changed. Mr. Elliott cautioned, however, that frequent changes in any annual filing requirements could be detrimental.

We agree with Mr. Elliott. We believe that a prudent utility should monitor its need for the gross-up and periodically determine if it is still warranted under that utility's particular circumstances. If circumstances have changed, it should be the utility's responsibility to notify this Commission. Accordingly, we find it appropriate to require those utilities that have received approval to use the gross-up to file a [illegible] statement with [illegible] whether circumstances have changed [illegible] the gross-up is [illegible]. If it is later discovered that the circumstances are not as reported by the utility, we can address the matter in a rate case or a separate investigation.

CALCULATION OF GROSS-UP

There are basically two methods of grossing-up, the full gross-up and the net present value (NPV) gross-up. The formulae for these methods are as follows:

Full Gross-up:

Depreciable Plant	(CP-(CP*(1/TL)*AR*.5)) * (1/(1-CTR))
Land	(CL*(1/(1-CTR)))

NPV Gross-up:

All Else	(CTR/(1-CTR))*((C+CP+CL)-((((C+CP)/TL)*(1-(1+ROR)-tl))/ROR)*(CTRi/CTR))

Where:

CP	=	Contributed plant
TL	=	Tax life for contributed plant
AR	=	Accelerated tax rate
CTR	=	Combined federal and state income tax rate
C	=	Contributed cash
CL	=	Contributed land
ROR	=	Utility's last allowed rate of return

-tl = Negative exponent of the tax life of the contributed asset
CTRi = Tax rate expected to be in effect when the depreciation is taken on the tax return

The full gross-up allows a utility to collect the full tax impact associated with CIAC, including the "tax-on-tax." The NPV gross-up allows a utility to collect the taxes associated with the gross-up less the present value of the tax depreciation that will be received in the future. By the very nature of the calculations, the full gross-up will provide more cash flow than the NPV method.

Both methods have advantages and disadvantages. The full gross-up would provide a ready source of cash to pay the maximum tax liability that would be associated with CIAC. However, the full gross-up method fails to take into account future depreciation that will be taken on the contributed assets. The NPV method takes into account the benefit of the future tax depreciation, but may not provide enough relief for a utility in a poor cash position. The NPV formula is also considered bulky, cumbersome, not easily understood, and subject to error.

We note that the formula for the full gross-up of depreciable plant takes into account the first year's tax depreciation using a half-year convention. We agree with Witness Elliott that, for purposes of the NPV gross-up, it should be assumed that utilities would utilize the most liberal method of tax depreciation allowed by the tax law and that, if they choose to use a method less favorable, it's simply to their detriment.

Based upon the evidence of record and the discussion above, we believe that both methods should be available to the utilities. However, we note that, out of the 44 utilities that requested the gross-up, only one implemented a NPV gross-up.

ACCOUNTING/REGULATORY TREATMENT - NO GROSS-UP

Taxes as Investment

All of the witnesses who addressed this issue agreed that, when a utility pays taxes associated with its collection of CIAC, it has, essentially, made an investment in such taxes. Witnesses

Elliott and Nixon testified that, if a utility does not gross-up, but pays the taxes related to its receipt of CIAC itself, we should include the full amount of its investment in such taxes in rate base, without regard to any used and useful considerations. Mr. Nixon also argued that any utility that is not authorized to gross-up is required to invest in taxes on CIAC. Accordingly, he argued that this places the utility and its customers at risk for the success of the development. Upon cross-examination, however, Mr. Nixon admitted that tax benefits follow the asset.

As mentioned above, there are certain tax benefits that flow from a utility's investment in taxes related to CIAC. Further, as discussed by Witness Elliott under cross examination, there are methods under which a utility may recover its carrying costs and earn a return on nonused and useful property, such as guaranteed revenue and allowance for funds prudently invested charges. Accordingly, we do not find it appropriate to allow utilities to earn a return on taxes related to nonused and useful CIAC.

Finally, we note Witness Nixon's concern that the debit-deferred balance will not be recognized in rate base, since we are moving to the formula (one-eighth of operating and maintenance expenses) method of calculating working capital. Accordingly, due to the long-lived nature of the assets involved, we find that debit-deferred taxes should be recognized separately from the working capital calculation.

Normalization

All witnesses who testified in this regard agreed that, if a utility does not gross-up, the tax effects of a its collection of CIAC should be normalized. By normalizing, the tax effects are recognized over the lives of the assets acquired.

Witness Causseaux testified that there are different methods to normalize. She recommends the method required by the IRS pursuant to Notice 87-82. Under Notice 87-82, debit deferred taxes should be treated as the regulatory body usually treats deferred taxes. In Florida, the norm is to offset debit deferred taxes against credit deferred taxes in the capital structure. If the net of the credit and debit deferred tax amounts is a debit, the amount is included in rate base.

Notwithstanding the above, Witness Causseaux stated that a more simplistic approach would be to recognize the full debit deferred tax balance in rate base. Witness Elliott, however, argued that the accounting treatment should follow the regulatory treatment, and not vice-versa. We agree. Although the proposed rate base treatment would be easier to administer, we believe that the appropriate method of normalization is the capital structure method. This would keep the treatment in total compliance with Notice 87-82.

ACCOUNTING/REGULATORY TREATMENT WITH GROSS-UP

All witnesses who testified regarding this issue also agreed that normalization accounting should be followed when a utility does gross-up. The IRS has no normalization requirements associated with CIAC that is grossed-up. However, we still believe that full normalization accounting should be utilized. This would result in consistent treatment between utilities that are not grossing-up and those that are. In addition, those utilities that switch from grossing-up to not grossing-up will maintain the same normalization methodology.

As discussed above, normalization involves offsetting debit-deferred taxes against credit-deferred taxes in the capital structure with any net debit-deferred balance included in rate base. Under the full gross-up method, the debit-deferred taxes would be fully offset by the contributed taxes. Under the NPV gross-up method, however, the utility would have an investment in the present value of the future tax depreciation.

Under either method of gross-up, a tax-on-tax will exist. Witnesses Elliott and Causseaux disagreed on how this should be treated. Witness Causseaux contended that the tax-on-tax is a permanent difference. As a permanent difference, it would flow through tax expense the year it is received. Witness Elliott, however, argued that the tax-on-tax is not a permanent difference. He argued that the tax-on-tax reverses over the useful life of the plant and that it reduces future tax expense.

We do not believe that it is important whether the tax-on-tax is a permanent difference or a timing difference by definition; what is important is who should receive the benefits. Based upon the evidence of record, we believe that the benefits should be passed back to the ratepayers over the lives of the related assets,

consistent with the theory of normalization. However, in order to identify the different contributions and to properly normalize, utilities will have to, and we find it appropriate to require them to, record the gross-up in a separate subaccount.

Offset of CIAC Income Against Net Operating Losses (NOLs)

By Order No. 21436, we proposed to require utilities to offset the tax impact of their collection of CIAC by their NOLs. Without exception, the utility witnesses argued that NOLs should not be used to offset the tax impact of CIAC.

The utilities argue that the collection of CIAC cannot create NOLs and that we should not, therefore, require them to offset CIAC-related taxes with losses generated by activities unrelated to their collection of CIAC. The utilities also argue that the NOLs should be reserved for those who bore the cost when the NOL was generated. Witness Deterding further argued that, since this Commission does not recognize NOLs as an investment, it should not recognize the tax benefits of NOLs either.

Witness Causseaux, on the other hand, argued that current tax expense is based upon jurisdictional operations and that, if a utility has NOLs, it will have no tax liability, regardless of the elements of revenues or expenses considered. Witness Elliott agreed that CIAC is not considered in isolation, but with all other transactions that occur. He also agreed that, no matter what our decision is in this docket, utilities will use their NOLs on their tax returns. In fact, according to Witness Deterding, when a gross-up is allowed, NOLs are or will be consumed more rapidly.

Based upon the evidence of record, we find it appropriate to require utilities to offset CIAC income against their NOLs. The purpose of this docket is to determine the treatment of the additional tax burden caused by the change in tax laws regarding CIAC. Until a tax liability is incurred, there is no additional tax burden. By requiring utilities to offset CIAC income with NOLs, we are only recognizing what they are actually doing on their tax returns. Further, such treatment is in keeping with the entire "tax picture", without isolating one piece - the taxation of CIAC.

Notwithstanding the above, we believe that a utility should only have to offset jurisdictional, above-the-line NOLs, and not below-the-line NOLs. This is consistent with our policy of

calculating taxes on a stand-alone basis. Below-the-line items would include, but not be limited to, the impact of disallowed expenses, nonused and useful plant depreciation, other expenses associated with nonused and useful plant, revenues associated with nonused and useful plant and interest associated with debt not included in the capital structure.

In addition to the above, the utilities also argue that, to the extent that their NOLs result from below-the-line losses, any required offset would be in violation of Section 367.081, Florida Statutes. Under Section 367.081(2)(a), Florida Statutes, in setting rates for utility service, "the commission shall consider the value and quality of the service and the cost of providing the service, which shall include, but not be limited to ... a fair return on the investment of the utility in property used and useful in the public service." (Emphasis added) Based upon the language just quoted, we believe that, although generally only above-the-line losses should be used to offset income from above-the-line operations, if an occasional below-the-line loss crept into the equation, we would not be in violation of Section 367.081, Florida Statutes.

Offset of CIAC Income Against Investment Tax Credits (ITCs)

The utility witnesses also do not believe that the tax liability resulting from the gross-up should be offset by ITCs. Witness Elliott argued that ITCs are economic assets, that ITC carry-forwards represent contingent receivables to the utility from the U.S. Treasury, and that it would, therefore, be inappropriate for us to deprive utilities of their use.

Witness Elliott also argued that the utility's collection of CIAC could not have given rise to the ITCs. Mr. Elliott explained that, prior to the tax law change, CIAC could not generate an ITC. Along with the changes in the tax laws, ITCs have effectively been eliminated. Mr. Elliott further argued that, to assign the benefit of an ITC carry-forward to the contributor creates an inequitable mismatch by giving the benefit to a party clearly not responsible for such benefit.

According to Witness Causseaux, however, utilities will use their ITCs to reduce taxable income from any source, including the receipt of CIAC or contributed taxes, without regard to the outcome of this docket, in order to minimize their actual tax liabilities.

As we have already stated, until there is an actual tax liability, we do not believe that there is any tax burden created by the collection of CIAC or contributed taxes. Our treatment will simply recognize what is actually transpiring.

Based upon the evidence of record, we find it appropriate to recognize, for regulatory purposes, the treatment afforded by the utilities themselves, [illegible] to offset CIAC income against ITCs. However, as with the decision regarding NOLs, we believe that only above-the-line ITCs should be used to offset.

Offset of NOLs and ITCs a Normalization Violation?

Witnesses Bowen, Deterding, Jackson and Wintz each testified that I.R.C. normalization requirements would be violated if the tax liability related to CIAC or the gross-up was offset by NOLs or ITCs. Witness Causseaux, however, did not believe that the requirements of Sections 46, 167, or 168, I.R.C., would be violated if NOLs and ITCs were used as an offset, so long as the appropriate normalization procedures are followed.

Witness Elliott testified that he did not believe that a refund of gross-up amounts due to the existence of NOLs or ITCs would violate the I.R.C. or the related regulations. In fact, he stated that, "[a]lthough the normalization requirements of the IRS are subject to the IRS' interpretation, I concur with Ms. Causseaux that refunding previously contributed taxes based upon the utilization of an NOL or ITC carry-forward would not represent a normalization violation if the investment in taxes is properly handled in the regulatory process."

Based upon the testimony of regulatory tax experts Causseaux and Elliott, we find that the normalization requirements of the I.R.C. and related regulations will not be violated by offsetting the tax liability associated with CIAC by regulatory NOLs and ITCs, if the utility properly records the transaction.

Tax Depreciation Benefits

Witnesses Elliott, Nixon, and Deterding each testified that, theoretically, the benefits of tax depreciation on CIAC should be passed back to the contributors of CIAC. These witnesses further testified, however, that because of practical considerations, such as prohibitive recordkeeping requirements, the benefits cannot be

returned to the contributors and must, therefore, be passed back to the general body of ratepayers. Although they did not sponsor any witnesses to support their position, SFCC and FHBA argued in their brief that, to the extent that a contributor pays the tax, the depreciation benefits should be passed back to him.

In her testimony, Witness Causseaux suggested that CIAC and the related taxes are ultimately borne by the homebuyer. Witness Elliott also testified to his belief that most developers treat CIAC costs as a cost of development, which is included in the total cost of the project. Witness Nixon does not agree.

Mr. Nixon testified that the prices which developers charge for homes are dictated by such factors as competition, area growth, interest rates and the resale market. He argued that, although developers presumably attempt to recover their costs and a profit through the purchase price, due to market conditions, the payment of CIAC-related taxes may actually reduce their profit margins. In support of this argument, he pointed out that a number of developers have objected to or complained about the gross-up.

We do not agree. Although market conditions may determine the selling price of a home, we believe that any time a developer has made a profit, it has recovered the costs of CIAC and the related taxes. Further, if the costs are passed on to the ultimate ratepayer, the contributor and the ratepayer are one and the same.

Since the practical considerations militate against passing the tax depreciation benefits back to developers and, since we believe that developers generally recover their costs, we find that the tax depreciation benefits should be passed back to the utility ratepayer. However, we note that, to the extent that utilities use the NPV method of grossing-up, they are passing the tax depreciation benefits of the gross-up back to developers, since the effect of that method is to offset the current taxes by the net present value of the future depreciation.

REFUND OF GROSS-UP AMOUNTS

The utilities do not believe that it would be fair and reasonable for this Commission to require refunds of the gross-up occasioned by the consumption of NOLs and ITCs. Witness Elliott

listed five reasons why he believes that this would be inappropriate.

First, Mr. Elliott argued that NOLs and ITCs are, for tax purposes, more or less equivalent to cash. Accordingly, he argues that it would be arbitrary for this Commission to treat them differently than it treats other economic assets.

We do not agree. The offset against NOLs and ITCs is merely a reflection of the way that the utilities will treat them for tax purposes. What Petitioners really object to here is that requiring them to refund all gross-up amounts collected in excess of their actual tax liabilities will deny them the opportunity to turn NOLs and ITCs into cash on hand.

Second, Mr. Elliott argues that the receipt of CIAC cannot create an NOL or ITC and that, to require refunds will assign such benefits to CIAC contributors, resulting in an inappropriate mismatch. We do not agree that the refund will assign the benefits to the contributors. The tax benefits are being used by the utilities to offset income. Again, what the utilities object to is the loss of the opportunity to cash-in on their NOLs and ITCs.

Third, Mr. Elliott argues that normalization must be followed when there is no gross-up or when excess amounts must be refunded, and that the refund of previously contributed taxes will result in increased revenue requirements. In fact, whenever NOLs or ITCs are consumed normalization will occur, whether or not there is a refund requirement. In addition, a refund requirement will only result in increased revenue requirements to the extent that a utility is earning below its last authorized rate of return.

Fourth, Mr. Elliott argues that a refund would be a windfall to those receiving it, at the expense of increased revenue requirements. We believe that, in fact, it is more likely a windfall to the utilities if they are not required to refund excess gross-up amounts, since they will receive cash now and the benefit of increased cash flow through depreciation over the lives of the assets. Further, we do not believe that it would be a windfall to the contributors if the refund is required, since both the utilities and the contributors were put on notice that a refund would be required by Order No. 16971, as follows:

> Monies in the CIAC Tax Impact Account may be withdrawn periodically for the purpose of paying that portion of the estimated Federal and State income tax expense which can be shown to be directly attributable to the repeal of Section 118(b) of the Internal Revenue Code and the inclusion of CIAC in taxable income. Annually, following the preparation and filing of the utility's annual, Federal and State income tax returns, a determination shall be made as to the actual Federal and State income tax expense that is directly attributable to the inclusion of CIAC in taxable income for the tax year. CIAC tax impact monies received during the tax year that are in excess of the actual amount of tax expense that is attributable to the receipt of CIAC, together with interest earned on such excess monies held in the CIAC Tax Impact Account must be refunded on a pro rata basis to the parties which made the contribution and paid the tax impact amounts during the tax year. (Order No. 16971, at page 3.)

This could be interpreted to mean that we will look at the receipt of CIAC as an isolated tax event, or that a tax liability must be incurred on the overall jurisdictional return. However, since the taxation of CIAC in isolation can only produce a tax liability, the former interpretation makes no sense because there is no way that a refund could occur. Accordingly, we believe that the intent was to consider the entire tax picture.

Fifth, Mr. Elliott argued that the application of a refund policy could become discriminatory due to potential fluctuations in CIAC collections from year to year. We agree that the potential for such "discrimination" exists. However, we do not find that any such discrepancies are either likely or likely to be "unfairly discriminatory," especially since any refunds will be based upon a rational and measurable basis - the utility's tax liability.

Finally, we note that the testimony of Mr. Charles deMenzes in this regard. Mr. deMenzes is the owner of Tradewinds Utilities, Inc. (Tradewinds), a small utility with NOLs that collects the gross-up. It appears from Mr. deMenzes' testimony that Tradewinds has a large percentage of nonused and useful plant and is having difficulty borrowing from banks. Mr. deMenzes was unequivocal about his desire to retain the gross-up as a trade-off for

Tradewinds' NOLs, in order to pay for operating expenses and expansion. Although we are sympathetic to Mr. deMenses' plight, the gross-up does have a specific purpose - payment of the tax liability associated with the collection of CIAC. There are other mechanisms available from this Commission to allow utilities in poor financial condition to earn a fair rate of return.

Based upon the evidence of record and our discussion above, we [illegible] refunded on a pro rata basis to those persons who contributed the taxes. Since a number of the utilities referred to in Order No. 21436 had NOLs and/or ITCs to offset CIAC-related income for 1987, they must refund gross-up amounts collected for 1987.

Notwithstanding the above, it appears from the record that some of the NOLs and ITCs used to offset taxes by Order No. 21436 were below-the-line items. These amounts were taken from the CIAC gross up reports required by Order No. 16971. Accordingly, to the extent these utilities can demonstrate that their losses or ITCs were below the line items, they should not be used to offset CIAC income. These utilities should, therefore, file amended reports to reflect only above-the-line NOLs and ITCs, with a reconciliation to the amounts originally filed. This suggestion would also hold true for 1988 and 1989 gross-up reports that have been filed. We also grant Staff administrative authority to process refunds of the gross-up based upon NOLs and ITCs for those years.

As for El Agua Corporation, Petitioners argue that its tax losses resulted from book/tax timing differences and that, to require it to refund contributed taxes would transfer the benefits of these book/tax timing differences from the ratepayers to the contributor. We do not agree. The book/tax timing difference would be accounted for through deferred tax accounting, regardless of whether or not a refund was required. Accordingly, it is not the book/tax timing difference, but the immediate benefit of converting the loss into cash that is actually being transferred from the utility back to those who contributed the cash.

With regard to Canal Utilities, Inc., Petitioners argue that its tax credits derive from ITC carry-forwards and that requiring it to offset CIAC-related taxes against the ITCs would transfer the benefits of the ITCs from the ratepayers to the contributors. This argument belies the fact that, as with the book/tax timing

differences discussed above, the ITCs would be normalized, for regulatory purposes, regardless of whether the refund is required or not. Again, the only benefit being transferred is the ability to convert ITCs into cash on hand.

Confiscation Without Due Process?

Finally, Petitioners argue that Order No. 21436 confiscates their property without due process of law. In this regard, we first point out that Order No. 21436 was protested and that the matter was considered at a Section 120.57(1), Florida Statutes, hearing. Since Order No. 21436 was protested, it became a legal nullity and cannot confiscate Petitioners' property. In addition, since it was considered in the context of an evidentiary hearing, Petitioners' due process rights have been protected.

Further, in a broader sense, offsetting CIAC income by NOLs and/or ITCs does not confiscate Petitioners' property. Petitioners will use these tax benefits on their tax returns regardless of the Commission's treatment. All we are doing by requiring a refund is recognizing this fact.

As already discussed, we believe that Petitioners really object to the fact that, by recognizing the actual tax transaction, they will be denied the opportunity to convert their losses and ITCs into cash on hand. Although our treatment will result in the consumption of these tax benefits for regulatory purposes, since contributions are now depreciable in any event, these benefits will be returned to the utilities as increased cash flow through depreciation over time. This would be recognized in ratemaking through deferred taxes. Accordingly, we do not believe that requiring the offset of NOLs and ITCs confiscates Petitioners' property in any sense of the term.

CONCLUSIONS OF LAW

1. This Commission is vested with jurisdiction over the gross-up of CIAC by the provisions of Sections 367.081, .091, .101, and .121, Florida Statutes.

2. The gross-up charges and conditions established herein are just and reasonable.

3. The requirements that utilities offset CIAC income against above-the-line NOLs and ITCs, and refund all amounts of gross-up collected in excess of their actual, jurisdictional tax liabilities resulting from their collection of CIAC, do not confiscate their property without just or fair compensation or violate their rights to due process.

Upon consideration of the foregoing, it is, therefore,

ORDERED by the Florida Public Service Commission that each of the findings contained in the body of this Order are approved in every respect. It is further

ORDERED that all matters discussed in the body of this Order are expressly incorporated herein by reference. It is further

ORDERED that no utility may gross-up CIAC without first obtaining the approval of this Commission. It is further

ORDERED that any utility that is currently grossing-up CIAC shall file a petition, in accordance with the provisions of this Order, for continued authority to gross-up no later than October 29, 1990. It is further

ORDERED that utilities shall follow the accounting procedures prescribed in the body of this Order whether they gross-up or not. It is further

ORDERED that utilities that do gross-up shall record the gross-up in a separate subaccount. It is further

ORDERED that all utilities that had below-the-line losses or ITCs for 1987, 1988, or 1989 shall file amended gross-up reports to reflect only above-the-line NOLs and ITCs, with a reconciliation to the amounts originally filed. It is further

ORDERED that any gross-up amounts collected in excess of a utility's actual tax liability resulting from its collection of CIAC, as set forth in the body of this Order, shall be refunded on a pro rata basis to the contributors of those amounts. It is further

ORDERED that Staff is hereby granted administrative authority to process refunds of the gross-up related to NOLs and ITCs for the years 1987, 1988, and 1989.

By ORDER of the Florida Public Service Commission, this 1st day of OCTOBER, 1990.

STEVE TRIBBLE, Director
Division of Records and Reporting

(S E A L)

RJP

State of Florida

ATTACHMENT 6

DIVISION OF LEGAL SERVICES
NOREEN S. DAVIS
DIRECTOR
(904) 487-2740

Public Service Commission

November 29, 1994

Mr. Martin Deterding, Esquire
Rose, Sundstrom & Bentley
2548 Blairstone Pines Drive
Tallahassee, FL 32301

Re: Martin Downs Utilities, Inc. Gross-Up Reports

Mr. Deterding:

This letter is in response to your inquiry dated November 15, 1994. Pursuant to the general provisions of Sections 367.011(1), 367.101, and 367.121(1), Florida Statutes, the Florida Public Service Commission (PSC) has jurisdiction over matters that arise during the life of a regulated utility. The PSC retains jurisdiction over all matters that arise during the life of the utility until those matters are resolved. Since the contributions-in-aid-of-construction (CIAC) gross-up is a matter that arose during the life of Martin Downs Utilities, Inc. (Martin Downs) and has not yet been resolved, the PSC continues to have jurisdiction over Martin Downs regarding gross-up issues.

Regarding the orders cited in your letter, it is true that a docket had not been opened to address the CIAC gross-up refunds when Order No. PSC-93-1484-FOF-WS was issued, acknowledging the sale of Martin Downs to Martin County. However, it is not a requirement that the order specifically mention CIAC gross-up refunds and continuing jurisdiction thereover for the PSC to retain jurisdiction.

I hope this letter clears up any misunderstanding that may surround this matter. If you have any further questions, please do not hesitate to contact me.

Sincerely,

Scott K. Edmonds
Staff Attorney

cc: Division of Water and Wastewater (Hill, Lowe, McCaskill, Iwenjiora)

ATTACHMENT 7

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Disposition of contributions-in-aid-of-construction (CIAC) funds received by Martin Downs Utilities, Inc., in Martin County during 1990, 1991, 1992, and 1993.	DOCKET NO. 931065-WS ORDER NO. PSC-97-1147-FOF-WS ISSUED: September 30, 1997

The following Commissioners participated in the disposition of this matter:

JULIA L. JOHNSON, Chairman
J. TERRY DEASON
SUSAN F. CLARK
DIANE K. KIESLING
JOE GARCIA

NOTICE OF PROPOSED AGENCY ACTION ORDER REQUIRING REFUNDS FOR THE YEARS 1989 THROUGH 1991 BUT DETERMINING THAT NO REFUNDS ARE REQUIRED FOR THE YEARS 1992 AND 1993

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

As a result of the repeal of Section 118(b) of the Internal Revenue Code, contributions-in-aid-of-construction (CIAC) became gross income and were depreciable for federal tax purposes. In 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.

Orders Nos. 16971 and 23541, issued December 18, 1986 and October 1, 1990, respectively, required utilities to 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. Those 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, be refunded on a pro rata basis to those persons who contributed the gross-up.

In Order No. 23541, this Commission required that any water and wastewater utility already collecting the gross-up on CIAC and wishing to continue, to file a petition for approval with the Commission on or before October 29, 1990. Martin Downs Utilities, Inc. (Martin Downs or utility) filed for authority to continue to gross-up on October 26, 1990. By Order No. 25360, issued November 19, 1991, Martin Downs was granted authority to continue to gross-up using the full gross-up formula.

On September 9, 1992, this Commission issued Proposed Agency Action Order No. PSC-92-0961-FOF-WS, which clarified the provisions of Orders Nos. 16971 and 23541 for the calculation of refunds of gross-up of CIAC. On September 14, 1992, Order No. PSC-92-0961A-FOF-WS, was issued which included Attachment A which reflected the generic calculation form. No protests were filed, and the Order became final.

Martin Downs was a Class A utility which provided service to approximately 3,486 water and 2,981 wastewater customers in Martin County. According to the 1992 annual report, operating revenues were reported as $1,112,379 for water and $1,040,717 for wastewater. The utility reported net operating income of $291,382 for the water system and $261,177 for the wastewater system.

Martin Downs facilities were sold to Martin County on August 12, 1993. By administrative Order No. PSC-93-1484-FOF-WS, in Docket No. 930818-WS, issued October 12, 1993, we acknowledged the transfer of the water and wastewater facilities and canceled Certificates Nos. 343-W and 301-S. The records of the Department of State show that Martin Downs was administratively dissolved as of August 25, 1995.

The disposition of CIAC gross-up collections was not addressed in Docket No. 930818-WS. However, we have jurisdiction to address the disposition of gross-up collections even though the facilities have been sold to the County. See, Charlotte County V. General Development Utilities, Inc., 653 So. 2d 1081 (Fla. 1st DCA 1995), discussed below.

Therefore, Docket No. 931065-WS was opened on November 4, 1993 to address the disposition of excess gross-up funds collected for the period of October 1, 1989 through August 12, 1993. We addressed the disposition of CIAC gross-up collections for the years ended December 31, 1987 through September 30, 1989, in Docket No. 910192-WS, Order No. 25388, issued November 25, 1991. Also, by letter dated November 23, 1993, our staff advised the attorney that had been representing Martin Downs that the collection of gross-up funds from October 1, 1989 through August 12, 1993, would be addressed. That letter referenced Orders Nos. 16971 and 23541.

At the May 30, 1995 Agenda Conference in the refund case of Canal Utilities, Inc. in Docket No. 941083-WS, questions were raised about whether or not our staff's method of calculating refunds was contrary to the requirements of Order No. 23541 and our previous practice. Also at issue, among others, was how prior years' depreciation on CIAC should be handled in determining the refund, and the offsetting of above-the-line net operating losses (NOLs) and investment tax credits (ITCs) with CIAC income. As a result of these issues, among others, we directed our staff to hold workshops to discuss the current practices we employed in dealing with the taxability of CIAC and to discuss viable alternatives. We also directed our staff to consider the need, if any, to change our current policy.

Workshops were held and comments and proposals were received from the industry and other interested parties. Pending the holding of these workshops and further guidance on the proper handling of CIAC gross-up cases, our staff temporarily delayed the processing of these types of cases. On March 29, 1996, we opened Docket No. 960397-WS to review our policy concerning the collection and refund of CIAC gross-up.

Pending this review, we directed, by Order No. PSC-96-0686-FOF-WS, issued on May 24, 1996, our staff to continue processing CIAC gross-up and refund cases pursuant to Orders Nos. 16971 and 23541; however, we also directed our staff, upon completion of its review of the proposals and comments offered by the workshop participants, to make a recommendation to us concerning whether our policy regarding the collection and refund of CIAC should be changed. In addition, we directed our staff to consider ways to simplify the process and determine whether there were viable alternatives to the gross-up.

However, the Small Business Job Protection Act of 1996 (The Act) was signed into law on August 20, 1996. The Act provided for the non-taxability of CIAC collected by water and wastewater utilities effective retroactively for amounts received after June 12, 1996. Consequently, we issued, on September 20, 1996, in Docket No. 960965-WS, Order No. PSC-96-1180-FOF-WS revoking the authority of utilities to collect gross-up of CIAC and cancelling the respective tariffs unless, within 30 days of the issuance of the Order, affected utilities requested a variance.

Because there was no longer a need to review our policy, we issued Order No. PSC-96-1253-FOF-WS on October 8, 1996, closing Docket No. 960397-WS. However, as established in Order No. PSC-96-0686-FOF-WS, all pending CIAC gross-up refund cases are still being processed pursuant to Orders Nos. 16971 and 23541. The purpose of this Order is to address the disposition of CIAC gross-up funds for Martin Downs for the period October 1, 1989 through August 12, 1993.

REFUND CALCULATIONS

Martin Downs was incorporated in the State of Florida in April 1981. Until January 26, 1990, Martin Downs was a wholly-owned subsidiary of Southern Realty Group, Inc. (SRG). On January 25, 1990, Martin Downs was recapitalized and then sold by SRG, to an entity controlled by certain SRG shareholders. On August 12, 1993, Martin County purchased the water and wastewater facilities from Martin Downs.

By administrative Order No. PSC-93-1484-FOF-WS, issued October 12, 1993, we canceled Martin Downs certificates and acknowledged the sale of the utility to an exempt governmental entity. Less than one month later, on November 4, 1993, we opened this docket to address any excess gross-up funds. In compliance with Order No. 16971, Martin Downs filed its CIAC reports for the fifteen-month period October 1, 1989 through December 31, 1990 and for the year ended December 31, 1991. By letter dated November 23, 1993, staff submitted its preliminary refund calculation numbers to the utility. In that letter, our staff specifically advised the utility that the preliminary analysis indicated that the utility had collected excess gross-up.

On December 16, 1993, the utility responded indicating that it disagreed with certain adjustments made by staff. Staff and the utility had several telephone discussions regarding the

differences. As a result, by letter dated October 11, 1994, our staff requested additional clarifying information. On January 12, 1995, the utility responded to staff's concerns with revised schedules and additional clarifying information.

By letter dated November 15, 1994, Martin Downs former shareholders inquired about whether the Commission had continuing jurisdiction over the CIAC gross-up refund now that the utility was being liquidated. By letter dated, November 29, 1994, counsel for the Commission advised Martin Downs that the Commission still had jurisdiction over the CIAC gross-up funds.

Martin Downs cited two orders in which the Commission acknowledged a sale and specifically addressed refunds associated with the utility. In Docket No. 940063-WS, involving Mid-Clay Services Corporation, Order No. PSC-94-0201-FOF-WS, issued February 18, 1997, canceled the utility's certificate. The order stated that a separate docket concerning the refund of excess gross-up funds had been opened: "Because the excess funds were collected prior to the sale to Clay County, Mid-Clay remains subject to our jurisdiction until all refunds have been made." Order No. PSC-94-0198-FOF-WS, issued February 17, 1994, in Docket No. 940051-WS, addressed a similar situation. However, in the case at hand, the docket concerning the refund of CIAC gross-up funds was not opened until after the issuance of the Order acknowledging transfer and canceling certificate.

We did not relinquish jurisdiction over Martin Downs in Order No. PSC-93-1484-FOF-WS as it relates to the refund of CIAC gross-up. As stated in the Mid-Clay order cited above, we retain jurisdiction over any matter which arose while the utility was under our jurisdiction. The gross-up funds were collected subject to refund prior to the cancellation of Martin Downs's certificates. Even though the order did not explicitly address the disposition of the gross-up funds, pursuant to Orders Nos. 16971 and 23541, and under our general authority, the disposition of those funds remained within our purview.

Our authority to address matters which occurred prior to the cancellation of a utility's certificate has been addressed in Charlotte County v. General Development Utilities, Inc., 653 So. 2d 1081 (Fla. 1st DCA 1995). Charlotte County claimed that the utility overbilled it for service. The complaint was filed after the sale of the utility and cancellation of its certificate, but involved overbilling which occurred prior to the sale and

cancellation. The Court held that the Commission had exclusive jurisdiction over the matter which occurred before the sale and cancellation of the certificate. The Court looked to the Commission's jurisdiction as defined by Section 367.011(2), Florida Statutes, and the definition of "utility" under Section 367.021(12), Florida Statutes.

Based on our continuing jurisdiction, our staff, by letter dated July 2, 1997, requested Martin Downs to respond to the following questions:

1. Are there any funds in the CIAC Tax Impact Account of MDU[Martin Downs]?

2. The CIAC Reports filed by MDU indicate that the utility collected $1,143,129 of gross-up for 1990 and $528,593 for 1991. How much was in the CIAC Tax Impact Account as of:

   a) August 11, 1995,

   b) October 12, 1993. (Corrected by telephone to October 12, 1995)

   If the amount in the account was less than the amount of gross-up collected, please explain how the difference was used.

3. On whose authority were the funds distributed?

4. Who (name and address) received and how much did they receive from distribution of the CIAC Tax Impact Account?

5. Is a record of the contributors of the gross-up available for 1990 and 1991?

By letter dated July 25, 1997, Steve Fry responded for the utility as follows:

1. Martin Downs Utilities, Inc. (MDU) sold all of its assets to Martin County. That sale was closed in August, 1993. Subsequent to the sale, MDU was dissolved and the MDU Liquidating Trust was established to liquidate the company.

2. The Public Service Commission (PSC) relinquished its jurisdiction in October, 1993. The PSC's Order did not reserve any jurisdiction over any MDU matters.

3. The last contact I had with the PSC was in early 1996.

4. The Liquidating Trust was terminated in late 1996.

5. Neither MDU nor the Liquidating Trust have any assets or employees, nor do they transact any business. There are no bank accounts.

6. Due to two floods that occurred in the building formerly occupied by this company, and the relocation of this office, the few remaining MDU files are in a state of general disorder.

Based on the foregoing, I cannot answer any of the questions described in your letter other than the first question, "Are there any funds in the CIAC Tax Impact Account of MDU?" That question is answered by number 5 above.

In reviewing the response, we do not agree with the assertions made in the first sentence of paragraph 2. above. Order No. PSC-93-1484-FOF-WS, issued on October 12, 1993, was an administrative order that merely acknowledged the sale (approved as a matter of right pursuant to Section 367.071(4)(a), Florida Statutes), canceled the certificates, and closed the docket. It did not address any continuing jurisdictional questions and said nothing about relinquishing jurisdiction. As stated previously (see analysis of the Charlotte County case above), we do not believe that it was necessary for the October 12 Order to specifically retain jurisdiction or advise Martin Downs that refunds of CIAC gross-up for the period from October 1, 1989, through the date of sale might be required. Section 367.011, Florida Statutes speaks for itself. Also, by opening Docket No. 931065-WS (opened November 4, 1993), by sending the November 23, 1993 letter, and by several other letters and meetings, we gave Martin Downs ample notice that the funds in the CIAC Tax Impact Account were still subject to refund. Also, Orders Nos. 16971 and 23541 specifically stated that the funds in this account would only be used to pay the taxes

associated with the collection of the CIAC gross-up or they would be refunded to the contributors.

Despite all this, the Liquidating Trust apparently distributed all funds without retaining at least the amount left in the CIAC Tax Impact Account to cover any possible refunds. Section 607.0834(1), Florida Statutes, specifically provides in pertinent part:

> A director who votes for or assents to a distribution made in violation of s. 607.06401 . . . is personally liable to the corporation for the amount of the distribution that exceeds what could have been distributed without violating s. 607.06401 . . . if it is established that he did not perform his duties in compliance with s. 607.0830.

Section 607.06401(3) provides in pertinent part:

> No distribution may be made, if after giving it effect: (a) The corporation would not be able to pay its debts as they become due in the usual course of business;

In this case the Liquidating Trust apparently distributed all funds without retaining any amounts whatsoever and without giving notice to the Commission. In order for a dissolved corporation to dispose of claims which are contingent, conditional, or unmatured, the corporation must, pursuant to Section 607.1406(4), Florida Statutes, give notice to the claimant. The Liquidating Trust did not appear to follow this procedure.

Also, Section 607.1406(13), Florida Statutes, states that a shareholder may be held liable for a claim against the corporation if a proceeding is begun prior to the expiration of three years following the effective date of dissolution. The effective date of dissolution appears to be August 25, 1995, and it appears that a proceeding against the shareholders could be brought as late as August 25, 1998.

Therefore, we have completed our analysis of the amount of CIAC gross-up funds that should be refunded. In every year reviewed, we made several adjustments to the utility's above-the-line computation. These adjustments are discussed below:

Management Fees, Accounting, Legal and Engineering Expenses: In its January 12, 1995 filing, for each year under consideration for gross-up refund disposition, the utility made adjustments to management fees, accounting, legal, and engineering expenses to reflect the amount that was established in its last rate case in Order No. 22869, issued April 27, 1990. In response, we note that the utility's annual reports for the period ended 1990 and 1991 show that the utility included the entire amount as regulatory expense. Further, upon review of the utility's annual report to determine whether it was overearning, the entire amount was considered to be utility related and used and useful. For annual report review purposes, these expenses were included and considered when determining the utility's net income. The utility's officer attests to the accuracy of the annual reports by signing them each year. Therefore, we find that the entire amount shall be included as above-the-line expense in calculating the utility's taxable income.

Based on the above, we have adjusted the above-mentioned expenses to reflect the amount that is consistent with the amount reported in the annual report for each period. This adjustment changed the utility's reported above-the-line taxable income/loss for both periods.

Depreciation Computed on Capacity Fees: The utility's calculation of first year depreciation expense was calculated based on the contributed property, and not capacity fees. The utility did not include the cash CIAC contributions in their calculation of depreciation, because cash is not depreciable property.

Rule 25-30.515(3), Florida Administrative Code, defines CIAC as:

> any amount or item of money, services, or property received by a utility, from any person or governmental agency, any portion of which is provided at no cost to the utility, which represents an addition or transfer to the capital of the utility, and which is utilized to offset the acquisition, improvement, or construction costs of the utility's property, facilities, or equipment used to provide utility services to the public. The term includes . . . system capacity charges, main extension charges and customer connection charges. (Emphasis added)

By definition, CIAC charges are intended for plant and are to be utilized for the acquisition, or construction of utility property; therefore, we find it is appropriate to assume the cash CIAC was converted into property in determining the amount of depreciation expense.

According to the utility's annual report, the utility added $3,167,750 of plant additions in 1990. The utility collected CIAC totaling $2,140,990, which consisted of $950,365 of property CIAC and $1,190,625 of cash CIAC. Plant additions exceeded the property and cash CIAC collections. Subtracting the amount of property CIAC from the total plant additions to determine how much cash CIAC was converted into plant, shows that all cash CIAC was converted. Using the Modified Accelerated Cost Recovery System (MACRS), the first year's depreciation for 1990 is calculated to be $64,167.

For 1991, however, it appears that only a portion of the cash CIAC was converted to plant. The utility collected CIAC totaling $1,073,666, which consisted of $527,633 of property CIAC and $546,033 of cash CIAC. However, according to the utility's annual report, the utility only added $829,982 of plant additions in 1991. Subtracting the property CIAC ($527,633) from the total plant additions ($829,982) indicates that the total cash CIAC converted to plant was only $302,349. Using the MACRS, the depreciation for 1991 was calculated to be $31,124.

Prior Years' CIAC Depreciation Classified Below-the-Line: The Commission classifies all prior year CIAC depreciation expense below-the-line. In its filing the only CIAC depreciation that the utility placed below-the-line was nonused and useful depreciation. Therefore, we have reclassified the prior year CIAC depreciation as a below-the-line expense.

ANNUAL GROSS-UP REFUND AMOUNTS

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 reports, supplemental information, and annual reports are reflected on Schedule No. 1. A summary of each year's refund calculation follows.

1990

The utility's 1990 CIAC report covers a fifteen-month period from October 1, 1989 through December 31, 1990. During this period the utility changed tax year end, recapitalized, and was sold to an entity controlled by certain SRG shareholders.

The utility proposed a refund of $3,854 for 1990 excess gross-up collections. The utility's refund is based, in part, on an above-the-line income of $178,969, before the inclusion of the taxable CIAC in income.

However, we calculate a refund of $32,361 for 1990, excluding accrued interest. Our calculation of above-the-line income includes the above-mentioned adjustments to the utility's above-the-line expenses. Also, in its filing, the utility classified $156,951 of its management fees and accounting, legal, and engineering expense below-the-line and $138,249 as above-the-line expense. The utility explained that its above-the-line amount agrees with the amount established in its last rate proceeding by Order No. 22869, issued April 27, 1990. In response, we note that the utility's annual report for 1990 and a prorated portion of the 1989 annual report shows that the utility included the entire $295,200 as an above-the-line expense. When the utility's annual report was reviewed to determine whether it was overearning, these expenses were included and considered when determining the utility's net income. Therefore, we have reclassified the entire $295,200 as an above-the-line expense, and included it in calculating the utility's taxable income.

With these adjustments, the utility's reported above-the-line taxable income of $178,969 was reduced to $69,306 before the inclusion of taxable CIAC income. Therefore, all taxable CIAC received during the year would still be taxed, net of first year's depreciation and CIAC that was collected but not grossed-up pursuant to contracts entered into before January 1, 1987.

The report indicates that a total of $1,143,129 of gross-up monies was collected for the CIAC that was grossed-up. According to the copy of the utility's CIAC journal account, the utility received taxable CIAC of $2,513,062 and deducted $16,879 for the first year's depreciation. We have deducted $607,847 for CIAC that was not grossed-up and $64,167 for the first year's depreciation on CIAC capacity and property collections. As a result, the net taxable CIAC was calculated to be $1,841,048. Using the 37.63%

combined marginal federal and state tax rates as provided in the 1990 CIAC Report, the tax effect is calculated to be $692,786. 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 $1,110,768.

Since the utility collected $1,143,129 in gross-up, the utility shall be required to refund $32,361 for 1990. This amount does not include the accrued interest which also must be refunded as of December 31, 1990, to the date of the refund.

1991

The utility proposes a refund of $15,234 for 1991 excess gross-up collections. The utility's refund is based on an above-the-line income of $63,790, before the inclusion of the taxable CIAC in income.

However, we calculate a refund of $22,064 for 1991, excluding accrued interest. Our calculation of above-the-line income includes the above-mentioned adjustments to the utility's above-the-line expenses. Also, in its filing, the utility classified $100,390 of its management fees and accounting, legal, and engineering expense below-the-line and $99,324 as above-the-line expense. The utility explained that its above-the-line amount agrees with the amount established in its last rate proceeding by Order No. 22869, issued April 27, 1990. In response, we note that the utility's annual report for 1991 shows that the utility included the entire $199,714 as an above-the-line expense. When the utility's annual report was reviewed to determine whether it was overearning, these expenses were included and considered when determining the utility's net income. Therefore, we have reclassified the entire $199,714 as an above-the-line expense, and included it in calculating the utility's taxable income.

With these adjustments, the utility's reported above-the-line taxable income of $63,790 was reduced to $42,488 before the inclusion of taxable CIAC income. Therefore, all taxable CIAC received during the year would still be taxed, net of first year's depreciation and CIAC that was collected but not grossed-up pursuant to contracts entered into before January 1, 1987.

The report indicates that a total of $528,593 of gross-up monies was collected for the CIAC that was grossed-up. The utility received taxable CIAC of $1,073,665 and deducted $19,786 for the

first year's depreciation. We have deducted $202,992 for CIAC that was not grossed-up and $31,124 for the first year's depreciation on CIAC capacity and property collections. As a result, the net taxable CIAC was calculated to be $839,549. Using the 37.63% combined marginal federal and state tax rates as provided in the 1991 CIAC Report, the tax effect is calculated to be $315,922. 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 $506,529.

Since the utility collected $528,593 in gross-up, the utility shall be required to refund $22,064 for 1991. This amount does not include the accrued interest which also must be refunded as of December 31, 1991 to the date of the refund.

1990 and 1991

Based on all the above, the utility shall refund $54,425, which consists of $32,361 for the fifteen-month period ending December 31, 1990, and $22,064 for fiscal year 1991, plus accrued interest through the date of the refund, for gross-up collected in excess of the tax liability resulting from the collection of CIAC. In accordance with Orders Nos. 16971 and 23541, all amounts for both 1990 and 1991 shall be refunded on a pro rata basis to those persons who contributed the taxes. The refund shall be completed within six months.

The utility shall submit copies of canceled checks, credits applied to monthly bills or other evidence which verifies that the refunds have been made, within 30 days from the date of the refund. Within 30 days from the date of the refund, the utility shall also provide a list of unclaimed refunds detailing contributor and amount, and an explanation of the efforts made to make the refunds. Further, the utility shall deliver any unclaimed refunds to the State of Florida Comptroller's Office as abandoned property. The unclaimed refunds shall be delivered to the Comptroller's office following our staff's written notification to the utility that the refunds have been made in accordance with this Order.

Because the utility has been dissolved, a copy of this Order requiring refunds shall be sent to Steve Fry, the representative of Martin Downs, and to Martin Downs's last counsel of record, F. Marshall Deterding. Also, a copy shall be sent to the former directors at their last known address.

1992 and 1993

Mr. James H. Anderson, Vice President of Martin Downs filed an affidavit which stated that the utility ceased collecting CIAC gross-up monies after December 31, 1991. Therefore, no refund is necessary for these last two years.

CLOSING OF DOCKET

Upon expiration of the protest period, if a timely protest is not filed by a substantially affected person, the docket shall remain open pending verification of the refund. Our staff shall be granted administrative authority to close the docket upon verification that the refunds have been made.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the provisions of this order are issued as proposed agency action and shall become final, unless a substantially affected person files an appropriate petition in the form provided by Rule 25-22.029, Florida Administrative Code, with the Director of the Division of Records and Reporting at 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the date set forth in the Notice of Further Proceedings below. It is further

ORDERED that Martin Downs Utilities, Inc., shall refund contributions-in-aid-of-construction gross-up funds in the amount of $32,361 for the fifteen-month period ending December 31, 1990, and $22,064 for fiscal year 1991, plus accrued interest through the date of refund, for gross-up collected in excess of the tax liability for those periods. It is further

ORDERED that, in accordance with Orders Nos. 16971 and 23541, all refund amounts shall be refunded on a pro rata basis to those persons who contributed the taxes. The refunds shall be completed within six months of the effective date of this order. Within thirty days from the date of the refund, Martin Downs Utilities, Inc., shall submit copies of cancelled checks, credits applied to monthly bills or other evidence that verifies that the utility has made the refunds. Within thirty days from the date of the refund, Martin Downs Utilities, Inc., shall also provide a list of unclaimed refunds detailing contributor and amount, and an explanation of the efforts made to make the refunds. It is further

ORDERED that, following staff's written notification to Martin Downs Utilities, Inc., that the refunds have been made in

accordance with this Order, the utility shall deliver the unclaimed refunds to the Comptroller's office. It is further

ORDERED that no refund is necessary for the years 1992 and 1993. It is further

ORDERED that all findings in this Order and the attachment thereto are incorporated and made a part of this Order. It is further

ORDERED that, upon expiration of the protest period, this docket shall remain open pending the verification of refunds. This docket shall be closed administratively upon verification that the refunds have been completed.

By ORDER of the Florida Public Service Commission this 30th day of September, 1997.

BLANCA S. BAYÓ, Director
Division of Records and Reporting

(S E A L)

RRJ

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 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on October 21, 1997.

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.

SCHEDULE NO. 1
MARTIN DOWNS UTILITIES, INC.

COMMISSION CALCULATED GROSS-UP REFUND

		1990	1991	1992
1	A-T-L Taxable Income Per Staff	$ 3,708,618	$ 1,624,960	$ N/A
2	Less CIAC	(2,513,062)	(1,073,665)	
3	Less Gross-up Collected	(1,143,129)	(528,593)	
4	Add First Year's Depr. on CIAC	16,879	19,786	
5	Add/Less Other Effects	0	0	
6				
7	Adjusted Income Before CIAC and Gross-up	$ 69,306)	$ 42,488	$
8				
9	Taxable CIAC	$ 2,513,062	$ 1,073,665	$
10				
11	Taxable CIAC Resulting in a Tax Liability	$ 1,905,215	$ 870,673	$
12	Less First Year's Depr.	(64,167)	(31,124)	
13				
14	Net Taxable CIAC	$ 1,841,048	$ 839,549	$
15	Combined marginal state and federal tax rate	37.63%	37.63%	
16				
17	Net Income Tax on CIAC	$ 692,786	$ 315,923	$
18	Less ITC Realized	0	0	
19				
20	Net Income Tax on CIAC	$ 692,786	$ 315,923	$
21	Expansion Factor for gross-up taxes	1.603334937	1.603334937	
22				
23	Gross-up Required to Pay Tax Effect	$ 1,110,768	$ 506,529	$
24	Less CIAC Gross-up Collected	(1,143,129)	(528,593)	
25				
26	(OVER) OR UNDER COLLECTION	$ (32,361)	$ (22,064)	$
27				
28				
29	TOTAL YEARLY REFUND	(32,361)	(22,064)	
30				
31				
32	PROPOSED REFUND (excluding interest)	(54,425)		
33				