State of Florida

Commissioners:
MICHAEL McK. WILSON, CHAIRMAN
THOMAS M. BEARD
BETTY EASLEY
GERALD L. (JERRY) GUNTER
JOHN T. HERNDON

Division of Appeals
David E. Smith, Director
(904) 488-7464

Public Service Commission

ORIGINAL FILE COPY

T

June 12, 1990

Mr. Carroll Webb
Joint Administrative Procedures
Committee
120 Holland Building
Tallahassee, Florida 32399

Re: DOCKET NO. 891278-PU, RULE 25-14.003

Dear Mr. Webb:

Enclosed are the following materials concerning the above referenced proposed rule:

1. A copy of the rule.
2. A copy of the F.A.W. notice.
3. A statement of facts and circumstances justifying the proposed rule.
4. A federal comparison statement.
5. A statement of the impact of the rule on small business.
6. An economic impact statement.

If there are any questions with respect to this rule, please ~~do not~~ hesitate to call on me.

Sincerely,

Cynthia B. Miller
Associate General Counsel

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

CBM:prl
Enclosures
cc: Steve Tribble, Director,
Division of Records & Reporting
4204G

DOCUMENT NUMBER-DATE
05178 JUN 12 1990
FPSC-RECORDS/REPORTING

Substantial rewording of Rule 25-14.003. See Florida Administrative Code for present text.

25-14.003 Corporate Income Tax Expense Adjustments.

The Commission shall monitor the impact of any corporate income tax expense changes upon the regulated companies' overall earnings through the Commission's ongoing earnings review program. The Commission may conduct a limited proceeding regarding such a change in tax expense or may address income tax adjustments in a full rate case.

The repeal of existing language shall not apply to pending cases.

The repeal of existing language shall apply to tax savings for tax year 1990 and thereafter.

Specific Authority: 350.127(2), 364.01, 366.05, 366.06(3), 367.121, F.S.

Law Implemented: 364.01, 364.035, 364.05, 366.05, 366.06, 366.076, 367.121, 367.081, 367.0822, F.S.

History: New 6/22/82, formerly 25-14.03, Amended.

CODING: Words underlined are additions; words in ~~struck-through~~ type are deletions from existing law.

FLORIDA PUBLIC SERVICE COMMISSION

Division of Appeals

DOCKET NO. 891278-PU

RULE TITLE: RULE NO.:

Corporate Income Tax Expense Adjustments 25-14.003

PURPOSE AND EFFECT: The intent of the proposed rule revision is to, in essence, repeal the existing cumbersome mechanism for corporate income tax expense adjustments; and to replace that mechanism with the existing ongoing earnings review mechanism.

SUMMARY: The rule revision would mandate that the Commission monitor the impact of any corporate income tax expense changes upon the regulated companies' overall earnings through the Commission's ongoing earnings review program. The Commission could address such a change in earnings through a limited proceeding or through a full rate case.

RULEMAKING AUTHORITY: 350.127(2), 364.01, 366.05, 366.06(3), 367.121, F.S.

LAW IMPLEMENTED: 364.01, 364.035, 364.05, 366.05, 366.06, 366.076, 367.121, 367.081, 367.0822, F.S.

SUMMARY OF THE ESTIMATE OF ECONOMIC IMPACT OF THIS RULE: The change applies existing Commission practice regarding ongoing earnings reviews to corporate income tax expense adjustments. Following rule revision, the Commission may conduct limited proceedings regarding any change in earnings due to tax rate changes or may address such earnings change through full rate cases. The proposed rule changes should increase Commission flexibility in dealing with changes in tax law without adding new agency costs or additional paperwork. Staff would continue to monitor utility earnings levels through surveillance reports, modified minimum filing requirements (MMFRs), and annual reports. Staff would bring recommendations to the Commission when a company's actual earned rate of return exceeded its authorized rate of return range. Utilities would benefit from the reduced reporting requirements.

WRITTEN COMMENTS OR SUGGESTIONS ON THE PROPOSED RULE MAY BE SUBMITTED TO THE FPSC, DIVISION OF RECORDS AND REPORTING, WITHIN 21 DAYS OF THE DATE OF THIS NOTICE FOR INCLUSION IN THE RECORD OF THE PROCEEDING. IF REQUESTED WITHIN 21 DAYS OF THE DATE OF THIS NOTICE, A HEARING WILL BE HELD AT THE DATE AND PLACE SHOWN BELOW:

TIME AND DATE: 9:30 A.M., July 18, 1990

PLACE: Room 122, 101 East Gaines Street, Tallahassee, Florida.

THE PERSON TO BE CONTACTED REGARDING THESE RULES AND THE ECONOMIC IMPACT STATEMENT IS: Director of Appeals, Florida Public Service Commission, 101 East Gaines Street, Tallahassee, Florida 32399

THE FULL TEXT OF THE RULE IS:

Substantial rewording of Rule 25-14.003. See Florida Administrative Code for present text.

25-14.003 Corporate Income Tax Expense Adjustments.

The Commission shall monitor the impact of any corporate income tax expense changes upon the regulated companies' overall earnings through the Commission's ongoing earnings review program. The Commission may conduct a limited proceeding regarding such a change in tax expense or may address income tax adjustments in a full rate case.

The repeal of existing language shall not apply to pending cases.

The repeal of existing language shall apply to tax savings for tax year 1990 and thereafter.

Specific Authority: 350.127(2), 364.01, 366.05, 366.06(3), 367.121, F.S.

Law Implemented: 364.01, 364.035, 364.05, 366.05, 366.06, 366.075, 367.121, 367.081, 367.0822, F.S.

History: New 6/22/82, formerly 25-14.03, Amended __________.

NAME OF PERSON ORIGINATING PROPOSED RULE: Ann Causseaux

NAME OF SUPERVISOR OR PERSON(S) WHO APPROVED THE PROPOSED RULES: Florida Public Service Commission

DATE PROPOSED RULES APPROVED: May 1, 1990

If any person decides to appeal any decision of the Commission with respect to any matter considered at the rulemaking hearing, if held, a record of the hearing is necessary. The appellant must ensure that a verbatim record, including testimony and evidence forming the basis of the appeal is made. The Commission usually makes a verbatim record of rulemaking hearings.

Rule 25-14.003
Docket No. 891278-PU

STATEMENT OF FACTS AND CIRCUMSTANCES JUSTIFYING RULE

The current mechanism for addressing corporate income tax expense adjustments has been cumbersome and ineffective. This version is intended to apply current Commission practices regarding the monitoring of companies' earnings.

STATEMENT ON FEDERAL STANDARDS

We are not aware of the existence of any federal standards which, pursuant to section 120.54(11)(a), are more or less restrictive than this proposed rule.

STATEMENT OF IMPACT ON SMALL BUSINESS

We do not believe there will be an impact on small businesses as defined by the statute.

RECEIVED

MAY 2 9 1990

General Counsel's Office
Florida Public Service Commission

M E M O R A N D U M

May 25, 1990

TO: DIVISION OF APPEALS (MILLER)

FROM: DIVISION OF RESEARCH (HEWITT) CH by PHW

SUBJECT: ECONOMIC IMPACT STATEMENT FOR DOCKET NO. 891278-PU REVISION OF RULE 25-14.003, FAC, CORPORATE INCOME TAX EXPENSE ADJUSTMENT RULE

SUMMARY OF THE RULE

Rule 25-14.003, FAC, was promulgated to establish policy and procedures for adjusting utility income tax expense when there are revisions in federal or state corporate income tax rates. Adjustments, in the form of customer refunds or additional collections, would generally be sufficient to adjust the rate of return (ROR) to the midpoint of the allowed range when the rate change causes the earnings to move through the midpoint. Exceptions would be when a utility is earning above the midpoint of its ROR range before a tax decrease or below the midpoint before a tax increase. Then, the adjustment would return it to the original achieved ROR.

In practice however, the current rule, by itself, has not had the intended results. Changes in the cost of capital and interest rates changed the return on equity (ROE) for utilities and made the mechanics of the rule ineffectual. Most utilities did not have overearnings after the federal tax decrease in 1986 and have not had to refund. Companies with overearnings have entered into stipulations with the Commission or have had hearings to establish new ROEs with the use of the 34 percent federal corporate tax rate in calculating any potential refunds.

The intent of the proposed rule revision is to eliminate ineffectual requirements and allow modified minimum filing requirements, surveillance reports, or annual reports to alert the Commission to overearnings after tax rate decreases. Limited proceedings, stipulations, earnings reviews, and more recent rate case hearings establish a current authorized rate of return on equity in determinations of tax savings refunds or deficiency collections. To this end, the proposed revisions of Rule 25-14.003 would eliminate most of the current language in the rule. Following rule revision, the Commission may conduct limited proceedings regarding any change in tax expense which has an impact on earnings or may address income tax changes in full rate cases or earnings review procedures.

DIRECT COSTS TO THE AGENCY

The proposed rule changes should increase Commission flexibility in dealing with changes in tax law without adding new agency costs or additional paperwork. The Commission receives modified minimum filing requirements, surveillance reports, and annual reports from selected utilities regardless of tax rate changes. Staff would continue to monitor utility earnings levels through these reports and bring recommendations to the Commission when a company's actual earned rate of return exceeded its authorized rate of return range.

COSTS AND BENEFITS TO THOSE PARTIES DIRECTLY AFFECTED BY THE RULE

The proposed revisions to Rule 25-14.003 would directly affect those utilities within the ratemaking scope of the Commission subject to federal or state income tax changes and the customers of those companies. Utilities would benefit from the reduced reporting requirements. Customers may benefit from having tax change adjustments based on the latest authorized rate of return on equity.

Discussions with Division of Auditing and Financial Analysis (DAFA) staff indicate recent Commission proceedings have resulted in lower rates of return on equity (ROEs) for purposes of the tax rule than those authorized in prior rate cases for the majority of affected utilities. All other things remaining equal, lower ROEs result in lower RORs, and subsequently larger refunds for ratepayers of affected utilities when tax rates decrease as in 1986.

Under the current rule, when tax rates decrease as in the Tax Reform Act of 1986, a profitable utility's tax expense decreases all other things being equal. The revenues resulting from tax savings that move a utility's ROR above the midpoint, must be refunded to the ratepayers. In reality, all things do not remain equal and determining tax savings and possible refunds is not a simple calculation.

If the utility is still at or below the midpoint of its allowed ROR after the tax rate change, there would be no refund. Because the Tax Reform Act of 1986 lowered the corporate income tax rate for subsequent years, affected utilities could be required to refund tax savings pursuant to FPSC rules in subsequent years until the new tax rate is embedded in revenue calculations. If corporate income tax rates increased under the current rule, ratepayers would be subjected to deficiency collections if a utility earned below the midpoint of its allowed range. These collections could continue in subsequent years until the new tax rate is embedded in revenue calculations.

As noted above, with the current rule, after the Tax Reform Act of 1986, most affected utility companies agreed to a new, lower ROE, for purposes of the tax rule that better reflected the recent cost of equity than that authorized in their last rate case. This practice has continued in subsequent years since revenue requirements for most companies were set based on a higher corporate income tax rate than presently applies to utility income; and refunds of overcollected revenues must be made until profitable companies undergo rate adjustments incorporating current corporate income tax rates.

For future tax rate increases (a movement in the opposite direction from the Tax Reform Act of 1986), after adoption of a current ROE, revision of the rule should decrease tax deficiencies and collections. If the most recent ROE was higher, refunds would be smaller and any collections larger.

In summary, costs associated with reporting requirements will decrease for the affected utilities and the opportunity to use the most current ROE in calculating any refunds or undercollections would more appropriately reflect current financial conditions.

IMPACT ON SMALL BUSINESSES

Many of the water and wastewater companies under ratemaking purview of the Commission are small businesses as defined in Chapter 120.54, Florida Statutes (1987) but because they are already exempt from the existing rule, they are not subject to the proposed changes.

IMPACT ON COMPETITION

Effects on interfirm or interindustry competition should be negligible since the proposed rule revisions essentially codify current Commission and utility practice. Therefore, the proposed revisions would be unlikely to change the relative competitive positions of the companies.

IMPACT ON EMPLOYMENT

Employment effects are expected to be minimal since the proposed rule revisions essentially codify current Commission and utility practice. However, if the amount of litigation or number of proceedings decrease, less industry resources would be spent on regulatory costs. Effects on employment of firms with inhouse regulatory expertise should be negligible since any decrease in proceedings from the proposed rule revisions would likely be absorbed within existing staff. Utilities which rely on consultants could decrease their demand for those resources but those firms are the ones least likely to need special proceedings under the current rule. Therefore, the proposed revisions would be unlikely to change the existing level of employment.

METHODOLOGY

Discussions were held with personnel from the Division of Auditing and Financial Analysis concerning the practices and conditions in the tax accounting of the affected businesses under the current rule and the consequences of revision; also staff from the various industry divisions were consulted. Rate of return and refund data from tax reports submitted by utilities were used in reviewing potential effects of this rule. Cost-benefit analysis was applied to determine effects of the proposed rule revisions. General microeconomic analysis was used to determine the effects on competition and effects on employment.

CH:jn/3673R