

MEMORANDUM

FEBRUARY 18, 1996

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FPSC-RECORDS/REPORTING

TO: DIVISION OF RECORDS AND REPORTING
FROM: DIVISION OF LEGAL SERVICES (CYRUS-WILLIAMS) *DCW*
RE: DOCKET NO. 961152-SU - APPLICATION FOR 1996 DISPOSITION
OF CONTRIBUTIONS IN AID OF CONSTRUCTION BY HUDSON
UTILITIES, INC. D/B/A HUDSON BAY COMPANY

0197-FOF

Attached is an ORDER NOTICE OF PROPOSED AGENCY ACTION ORDER FINDING REFUND REQUIRED FOR 1993 AND 1994, with attachments, to be issued in the above-referenced docket. (Number of pages in Order - 10)

SS

DCW/dp

Attachment

cc: Division of Water and Wastewater (Johnson)

I: 961152OR.DCW

Attachments Not on-line

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Application for 1996) DOCKET NO. 961152-SU
disposition of contributions in) ORDER NO. PSC-97-0197-FOF-SU
aid of construction by Hudson) ISSUED: February 19, 1997
Utilities, Inc. d/b/a Hudson Bay)
Company.)
_____)

The following Commissioners participated in the disposition of this matter:

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

NOTICE OF PROPOSED AGENCY ACTION
ORDER FINDING REFUND REQUIRED FOR 1993 AND 1994

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 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, the Commission 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.

Order Nos. 16971, issued December 18, 1986, and 23541, issued October 1, 1990, require that utilities annually file information which would be used to determine the actual state and federal income tax liability directly attributable to the CIAC. The information would also determine whether refunds of gross-up would be appropriate. These orders also require 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 taxes.

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FPSC RECORDS/REPORTING

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In Order No. 23541, the Commission required 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. On November 30, 1992, pursuant to Order No. 23541, Hudson Utilities, Inc. (Hudson or utility) filed for initial authority to gross-up CIAC. The information as filed met the filing requirements of Order No. 23541. By order No. PSC-93-0206-FOF-SU, issued February 9, 1993, the Commission allowed the utility's proposed tariff to become effective by operation of law on an interim basis for gross-up on CIAC. Order No. PSC-93-0962-FOF-SU, issued June 28, 1993, granted Hudson authority to gross-up.

Hudson is a Class B wastewater utility providing service in Pasco County. As of December 31, 1995, the utility served 1,172 wastewater customers. The utility had gross operating revenues of \$629,192 for the wastewater system. The utility reported a net operating income of \$17,394 for the wastewater system.

On September 9, 1992, this Commission issued Proposed Agency Action Order No. PSC-92-0961-FOF-WS, which clarified the provision 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, reflecting the generic calculation form. On October 12, 1994, Order No. PSC-94-1265-FOF-WS revised the full gross-up formula.

On March 29, 1996, Docket No. 960397-WS was opened to review the Commission's policy concerning the collection and refund of CIAC gross-up. Workshops were held and comments and proposals were received from the industry and other interested parties. By Order No. PSC-96-0686-FOF-WS, issued May 24, 1996, Commission staff was directed to continue processing CIAC gross-up and refund cases pursuant to Order Nos. 16971 and 23541; to make a recommendation to the Commission concerning whether the Commission's policy regarding the collection and refund of CIAC should be changed upon the staff's completion of its review of the proposals and comments offered by the workshop participants; and to consider ways to simplify the process and determine whether there were viable alternatives to the gross-up.

However, on August 1, 1996, the Small Business Job Protection Act of 1996 (the Act) was signed into law by the President 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. As a result, on September 20, 1996, in Docket No. 960965-WS, Order No. PSC-96-1180-FOF-WS was issued to revoke the authority of utilities

to collect gross-up of CIAC and to cancel the respective tariffs unless, within 30 days of the issuance of the order, affected utilities requested a variance. Docket No. 960397-WS was also closed on October 8, 1996. As established in Order No. PSC-0686-FOF-WS, all pending CIAC gross-up refund cases are being processed pursuant to Order Nos. 16971 and 23541.

On October 18, 1996, Hudson requested a variance from Order No. PSC-96-1180-FOF-WS. The utility stated that because in 1994 and 1995 it established an installment payment plan to allow customers to pay the applicable service availability charge plus the CIAC gross-up tax on a 24-month installment plan, it needed a variance to collect the remaining installment payments, including the CIAC gross-up tax. Order No. PSC-97-0040-FOF-SU, issued January 9, 1997 in Docket No. 961270-SU, granted the utility's request for variance.

This order addresses the disposition of the gross-up of CIAC collected by Hudson for each of the years 1993 and 1994.

Refund Calculations for Years 1993 and 1994

In compliance with Order No. 16971, Hudson filed annual CIAC gross-up reports for 1993 and 1994. Our calculations, taken from these gross-up reports, are reflected on Schedule No. 1, which is attached hereto and by reference incorporated herein. Gross-up calculations are in accordance with the method adopted in Order No. PSC-92-0961-FOF-WS. A summary of each year's calculations follows.

1993

The utility's 1993 CIAC report indicates the utility was in an above-the-line taxable position prior to the inclusion of taxable CIAC in income. Therefore, all taxable CIAC received would be taxed, net of the first year's depreciation.

The CIAC report indicates that a total of \$87,000 in taxable CIAC was received, with \$3,491 being deducted for the first year's depreciation. As a result, net taxable CIAC was calculated to be \$83,509. The combined marginal federal and state tax rate of 37.63% was used to calculate the tax effect of \$50,383, as provided in the utility's 1993 CIAC report. The utility collected \$52,200 of gross-up monies; therefore, our calculations show that the utility collected \$1,817 more in gross-up than is required to pay the tax impact, and a refund of \$1,817 is required.

The utility agrees that a refund of \$1,817 is appropriate, but proposes the recovery of \$5,030 in cost for preparing the refund report in 1993. However, we have excluded the accounting costs for preparing the refund report from the refund calculation for several reasons. First, the utility is attempting to mix pre-tax and post-tax amounts. Second, Orders Nos. 16971 and 23541 do not provide for the netting of costs incurred with filing refund reports with the excess gross-up collections. Order No. 23541 specifically states:

[A]ll gross-up amounts in excess of a utility's actual tax liability resulting from its collection of CIAC should be refunded on a pro rata basis to those persons who contributed the taxes.

Accordingly, the contributors shall not be held responsible for the accounting costs incurred to determine the amount of each customer's refund. Although these costs were incurred to satisfy regulatory requirements, a reduction of the contributors' refund amount is not the appropriate place to seek recovery of accounting charges. The utility may seek recovery of these expenses in a rate case proceeding.

In addition, we find that in no instance should maintenance and administrative costs associated with any refund be borne by the customers. Those costs are the responsibility of, and should be borne by, the utility. Accordingly, we find that a refund of \$1,817 is required for 1993, plus accrued interest through the date of refund.

1994

Order No. PSC-95-0376-FOF-SU, issued March 16, 1995 in Docket No. 950052, gave the utility authority to provide customers the option of paying the CIAC and the gross-up charge in installment payments. The installment payment plan allowed the contributor to pay the service availability charge of \$1,000 plus the gross-up taxes of \$600 in 24 monthly installment payments. In 1994 the utility collected CIAC and gross-up from 396 customers. Three hundred and thirty seven (337) customers paid the CIAC and gross-up in full and the remaining 59 customers signed notes to pay the CIAC and gross-up on the installment plan. For federal income tax purposes for 1994, however, the utility reported all of the CIAC and gross-up as income whether or not it was paid in full or in installments.

Therefore, in calculating the appropriate refund amount for 1994, we did not utilize the generic refund calculation form established in Order No. PSC-92-0961A-FOF-WS in order to recognize the fact that some customers paid the gross-up in full, while others paid the gross-up in installments. The utility calculated a refund of \$43,008 using the generic refund calculation form, less \$6,476 to reflect recovery of the cost of preparing the refund. However, this calculation understates the amount of CIAC and gross-up that should have been collected in 1994. Further, as discussed previously, the contributors shall not be held responsible for the accounting costs incurred to determine the amount of each customer's refund.

The utility's 1994 CIAC report indicates the utility had an above-the-line loss of \$75,488 prior to the inclusion of taxable CIAC in income. As a result, all of the CIAC collected would not be taxed. Order No. 23541 requires that above-the-line losses be offset against CIAC income. Therefore, the above-the-line loss of \$75,488 must be netted with the taxable CIAC collected.

The CIAC report indicates that the utility collected \$396,000 of taxable CIAC, with \$18,338 being deducted for the first year's depreciation. As a result, the amount of taxable CIAC is calculated to be \$377,662. When this amount is offset with the above-the-line loss of \$75,488, net taxable CIAC is calculated to be \$302,174. The combined marginal federal and state tax rate of 37.63% was used to calculate the tax effect of \$113,708. 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 \$182,312. Based on this amount, the utility should have collected \$460.38 ($\$182,312/396$) of gross-up from each customer.

The CIAC report indicates that the utility collected \$202,200 of gross-up from the 337 customers who paid the gross-up in full. However, based on the amount of gross-up required to pay the taxes on the CIAC, the utility should have only collected \$155,148.06 ($\460.38×337) from those customers. Therefore, the customers who paid the gross-up in full are due a refund of \$47,051.94 or \$139.62 per customer, plus accrued interest through the date of refund. Because of the installment payment plan, the utility only collected \$14,000 of gross-up in 1994 from the customers who paid the gross-up in installments. The utility, therefore, may collect a total of \$27,162.42 ($\460.38×59) from those customers.

According to Orders Nos. 16971 and 23541, all amounts shall be refunded on a pro rata basis to those persons who contributed the taxes. The refunds shall be completed within 6 months of the

effective date of this order. Within 30 days from the date of the refund, the utility shall submit copies of cancelled checks, credits applied to monthly bills or other evidence that verifies that the utility has made the refunds, the utility also shall provide a list of unclaimed refunds detailing contributor and amount, and an explanation of the efforts made to make the refunds.

Closing of Docket

Upon expiration of the protest period, if a timely protest is not filed by a substantially affected person, this docket shall remain open pending completion and verification of the refunds. Upon verification that the refunds have been made, this docket shall be closed administratively.

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 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 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 each of the findings made in the body of this order is hereby approved in every respect. It is further

ORDERED that all matters contained in the schedules attached hereto are by reference incorporated herein. It is further

ORDERED that Hudson Utilities, Inc. shall refund \$1,817, plus accrued interest through the date of refund, for gross-up collected in excess of the tax liability for 1993. It is further

ORDERED that Hudson Utilities, Inc. shall refund \$47,051.94, plus accrued interest through the date of refund, to contributors who paid the gross-up in full in 1994 for gross-up collected in excess of the tax liability. It is further

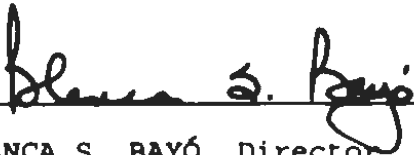
ORDERED that all refund amounts shall be refunded on a pro rata basis to those persons who contributed the taxes. The refunds shall be completed within 6 months of the effective date of this order. Within 30 days from the date of the refund, the utility shall submit copies of cancelled checks, credits applied to monthly

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bills or other evidence that verifies that the utility has made the refunds, the utility also shall 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 upon expiration of the protest period, this docket shall remain open pending 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 19th day of February, 1997.



BLANCA S. BAYÓ, Director
Division of Records and Reporting

(S E A L)

DCW

Commissioner Deason and Commissioner Kiesling dissented on the issue of whether the utility should be allowed to offset the accounting costs incurred to determine the amount of each customer's refund against the actual amount to be refunded.

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.

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 March 12, 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.

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SCHEDULE NO. 1

COMMISSION APPROVED CALCULATED GROSS-UP REFUND

HUDSON UTILITIES, INC.

SOURCE: (Line references are from CIAC Reports)

	<u>1993</u>	<u>1994</u>
1 Form 1120, Line 30 (Line 15)	\$ 159,404	\$ 518,374
2 Less CIAC (Line 7)	(87,000)	(396,000)
3 Less Gross-up collected (Line 19)	(52,200)	(216,200)
4 Add First Year's Depr on CIAC (Line 8)	3,491	18,338
5 Add/Less Other Effects (Lines 20 & 21)	0	0
6		
7 Adjusted Income Before CIAC and Gross-up	\$ 23,695	\$ (75,488)
8 Taxable CIAC (Line 7)	87,000	396,000
9 Less first years depr. (Line 8)	(3,491)	(18,338)
10		
11 Taxable CIAC Resulting in a Tax Liability	\$ 83,509	\$ 302,174
12 Less: NOL Carryforward	0	0
13		
14 Net Taxable CIAC	\$ 83,509	\$ 302,174
15 Effective state and federal tax rate	37.63%	37.63%
16		
17 Net Income tax on CIAC	\$ 31,424	\$ 113,708
18 Less ITC Realized	0	0
19		
20 Net Income Tax	\$ 31,424	\$ 113,708
21 Expansion Factor for gross-up taxes	1.603334937	1.603334937
22		
23 Gross-up Required to pay tax effect	\$ 50,383	\$ 182,312
24 Less CIAC Gross-up collected (Line 19)	(52,200)	(218,200)
25		
26 (OVER) OR UNDER COLLECTION	\$ (1,817)	\$ (33,888)
27	=====	=====
28		
29 TOTAL YEARLY REFUND	\$ (1,817)	\$ (33,888)
30	=====	=====
31		
32 PROPOSED REFUND (excluding interest)	\$ (35,705)	
33	=====	

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SCHEDULE-2

BREAK DOWN BASED ON CUSTOMERS & CIAC

HUDSON UTILITIES, INC.

		1994	
	NOTES	PAID IN FULL	TOTAL
1 Taxable CIAC Resulting in a Tax Liability	\$ 45,024	257,150	302,174
2 Less: NOL Carryforward	0	0	0
3			
4 Net Taxable CIAC	\$ 45,024	257,150	302,174
5 Effective state and federal tax rate	37.63%	37.63%	37.63%
6			
7 Net Income tax on CIAC	\$ 16,943	96,766	113,709
8 Less ITC Realized			
9			
10 Net Income Tax	\$ 16,943	96,766	113,709
11 Expansion Factor for gross-up taxes	1.603334937	1.603334937	
12			
13 Gross-up Required to pay tax effect	\$ 27,165	155,148	182,313
14 Less CIAC Gross-up collected (Line 19)	(14,000)	(202,200)	(216,200)
15			
16 (OVER) OR UNDER COLLECTION	\$ 13,165	(47,052)	(33,887)
17			
18			
19 TOTAL YEARLY REFUND	\$ 13,165	(47,052)	(33,887)
20			
21			
22 PROPOSED REFUND (excluding interest)	\$ (47,052)		
23			