**FLORIDA PUBLIC SERVICE COMMISSION**

**Fletcher Building**

**101 East Gaines Street**

**Tallahassee, Florida 32399-0850**

**M E M O R A N D U M**

**May 6, 1993**

**TO : DIRECTOR, DIVISION OF RECORDS AND REPORTING**

**FROM : DIVISION OF WATER AND WASTEWATER (MEADOR)**

**DIVISION OF LEGAL SERVICES (FEIL)**

**RE : UTILITY: KINGSLEY SERVICE COMPANY**

**DOCKET NO. : 930217-WS**

**COUNTY : CLAY COUNTY**

**CASE : DISPOSITION OF GROSS-UP FUNDS COLLECTED**

**AGENDA : 5/18/93 - CONTROVERSIAL - PROPOSED AGENCY ACTION - PARTIES MAY PARTICIPATE**

**CRITICAL DATES: NONE**

**RECOMMENDATION FILE NAME: I:\PSC\WAW\WP\930217.RCM**

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**CASE BACKGROUND**

The repeal of Section 118(b) of the Internal Revenue Code (I.R.C.) resulted in making contributions-in-aid-of-construction (CIAC) gross income and 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.

Orders 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, and whether a refund of the gross-up is appropriate for any given year for which gross-up was in effect. These orders also required that all gross-up amounts for a tax year which are in excess of a utility's actual tax liability for the same year resulting from its collection of CIAC should be refunded on a pro rata basis to those persons who contributed the taxes.

In Order No. 23541, the Commission determined that any water and wastewater utility already collecting the gross-up on CIAC and wishing to continue collecting the gross-up, had to file a petition for approval with the Commission on or before October 29, 1990. By Order No. 25505 Kingsley Service Company (Kingsley or Utility) was authorized to continue to gross-up CIAC for the related tax impact. The Utility was authorized a partial gross-up percentage of 25.17% because of its cost effectiveness and equitable allocation of the tax burden between the utility and developers.

On September 9, 1992, this Commission issued PAA 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 on September 9, 1992, which included Attachment A which reflects the generic calculation form. No protests were filed, and the Order became final.

Kingsley is a Class A utility which provides water and wastewater service to customers in Clay County. According to their 1991 annual report, operating revenue of $1,770,334 for water and $2,612,022 for the wastewater system were reported. The utility reported net operating income of $285,698 for the water system and $224,104 for the wastewater system.

**DISCUSSION OF ISSUES**

**ISSUE 1:** Should Kingsley Service Company be required to refund excess gross-up collections plus accrued interest through the date of refund?

**RECOMMENDATION:** No, the utility did not collect gross-up in excess of its tax liability, and no further action is required. (MEADOR)

**STAFF ANALYSIS:** In compliance with Order No. 16971, Kingsley filed its 1987 through 1992 annual CIAC reports regarding its collection of gross-up for each year. In response to staff's preliminary calculations, the utility submitted copies of IRS examination reports for each year 1987 through 1990. Using the amounts from the IRS examination reports, the utility recalculated our preliminary gross-up calculations. The revised calculations show that no refund is due.

**ANNUAL GROSS-UP REFUND AMOUNTS**

Based upon the foregoing, staff has calculated the amount of refund per year which is appropriate. Our calculations, taken from the information provided by the utility in its gross-up reports and the IRS examination reports for each year are reflected on Schedule No. 1. Based upon the IRS examination findings, no refund is due for any year, 1987 through 1992. A summary of each year's calculation follows.

**1987**

Staff calculates that no refund is due for 1987. The 1987 CIAC report and IRS examination report indicate that a total of $19,720 of gross-up collections were received, with the first year's depreciation reported as $980. Staff has used the 43.30% combined federal and state tax rate as provided in the 1987 CIAC Report to calculate the tax effect. Based upon the foregoing, staff calculates gross-up required of $22,547 with gross-up collections of $19,720. The utility did not collect gross-up in excess of its tax liability, therefore, no further action is necessary for 1987.

**1988**

Staff calculates that no refund is due for 1988. The 1988 CIAC report and IRS examination report indicate that a total of $452,382 of gross-up collections were received, with the first year's depreciation reported as $41,598. Staff has used the 37.63% combined federal and state tax rate as provided in the 1988 CIAC Report to calculate the tax effect. Based upon the foregoing, staff calculates gross-up required of $644,772 with gross-up collections of $452,382. The utility did not collect gross-up in excess of its tax liability, therefore, no further action is necessary for 1988.

**1989**

Staff calculates that no refund is due for 1989. The 1989 CIAC report and IRS examination report indicate that a total of $344,706 of gross-up collections were received, with the first year's depreciation reported as $27,418. Staff has used the 37.63% combined federal and state tax rate as provided in the 1989 CIAC Report to calculate the tax effect. Based upon the foregoing, staff calculates gross-up required of $424,586 with gross-up collections of $344,706. The utility did not collect gross-up in excess of its tax liability, therefore, no further action is necessary for 1989.

**1990**

During 1990, the utility was granted authority to continue to gross-up, however, the utility requested, and the Commission approved, use of the full gross-up method at a reduced or partial percentage of 25.17%. In determining the combined 1990 refund calculation, staff took all 1990 totals and divided them in half. One half of the calculation utilized the full gross-up expansion factor, while the second half utilized the partial gross-up expansion factor. For both the first six months as well as the last six months of 1990, our calculation shows that the amount of gross-up required to pay the tax liability exceeded the amount of gross-up collected.

Staff calculates that no refund is due for 1990. The 1990 CIAC report and IRS examination report indicate that a total of $340,943 of gross-up collections were received, with the first year's depreciation reported as $28,314. Staff has used the 37.63% combined federal and state tax rate as provided in the 1990 CIAC Report to calculate the tax effect. Based upon the foregoing, staff calculates gross-up required of $443,987 with gross-up collections of $340,943. The utility did not collect gross-up in excess of its tax liability, therefore, no further action is necessary for 1990.

**1991**

Staff calculates that no refund is due for 1991. The 1991 CIAC report and IRS examination report indicate that a total of $152,269 of gross-up collections were received, with the first year's depreciation reported as $23,218. Staff has used the 37.63% combined federal and state tax rate as provided in the 1991 CIAC Report to calculate the tax effect. Based upon the foregoing, staff calculates gross-up required of $280,691 with gross-up collections of $152,269. The utility did not collect gross-up in excess of its tax liability, therefore, no further action is necessary for 1991.

**1992**

Staff calculates that no refund is due for 1992. The 1992 CIAC report and IRS examination report indicate that a total of $146,517 of gross-up collections were received, with the first year's depreciation reported as $18,532. Staff has used the 37.63% combined federal and state tax rate as provided in the 1992 CIAC Report to calculate the tax effect. Based upon the foregoing, staff calculates gross-up required of $224,034 with gross-up collections of $146,517. The utility did not collect gross-up in excess of its tax liability, therefore, no further action is necessary for 1992.

**ISSUE 2:** Should the docket be closed?

**RECOMMENDATION:** Yes, the docket should be closed upon expiration of the protest period. (MEADOR, FEIL)

**STAFF ANALYSIS:** Staff believes this docket should be closed if a timely protest is not filed.

KINGSLEY SERVICE COMPANY STAFF CALCULATED GROSS‑UP REFUND

SOURCE: (Line references are from CIAC Reports)

COMBINED Full G‑up Partial G‑up

1987 1988 1989 1990 1991 1992 1990 1990

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1 Form 1120, Line 30 (Line 15) $ 906,131 $ 2,000,247 $ 1,323,044 $ 1,271,626 $ 896,574 $ 1,365,991 $ 635,813 $ 635,813

2 Less CIAC (Line 7) (30,504) (1,110,276) (731,150) (855,417) (619,147) (494,174) (427,709) (427,709)

3 Less Gross‑up collected (Line 19) (19,720) (452,382) (344,706) (340,943) (152,269) (146,517) (170,471) (170,471)

4 Add First Year's Depr on CIAC (Line 8) 980 41,598 27,418 28,314 23,218 18,532 14,157 14,157

5 Add/Less Other Effects (Lines 20 & 21) 0 0 0 14,245 0 0 7,122 7,122

6 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

7 Adjusted Income Before CIAC and Gross‑up $ 856,888 $ 479,187 $ 274,606 $ 117,825 $ 148,377 $ 743,830 $ 58,912 $ 58,912

8

9 Taxable CIAC (Line 7) $ 30,504 $ 1,110,276 $ 731,150 $ 855,417 $ 619,147 $ 494,174 $ 427,709 $ 427,709

10

11 Taxable CIAC Resulting in a Tax Liability $ 30,504 $ 1,110,276 $ 731,150 $ 855,417 $ 619,147 $ 494,174 $ 427,417 $ 427,417

12 Less first years depr. (Line 8) (980) (41,598) (27,418) (28,314) (23,218) (18,532) (14,157) (14,157)

13 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

14 Net Taxable CIAC $ 29,524 $ 1,068,678 $ 703,732 $ 827,103 $ 595,929 $ 475,642 $ 413,260 $ 413,260

15 Effective state and federal tax rate 43.30% 37.63% 37.63% 37.63% 37.63% 37.63% 37.63% 37.63%

16 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

17 Net Income tax on CIAC $ 12,784 $ 402,144 $ 264,814 $ 311,239 $ 224,248 $ 178,984 $ 155,510 $ 155,510

18 Less ITC Realized 0 0 0 0 0 0 0 0

19 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

20 Net Income Tax $ 12,784 $ 402,144 $ 264,814 $ 311,239 $ 224,248 $ 178,984 $ 155,510 $ 155,510

21 Expansion Factor for gross‑up taxes 1.76366843 1.603334937 1.603334937 1.2517 1.2517 1.603334937 1.2517

22 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

23 Gross‑up Required to pay tax effect $ 22,547 $ 644,772 $ 424,586 $ 443,987 $ 280,691 $ 224,034 $ 249,335 $ 194,652

24 Less CIAC Gross‑up collected (Line 19) (19,720) (452,382) (344,706) (340,943) (152,269) (146,517) (170,471) (170,471)

25 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

26 PROPOSED REFUND (excluding interest) $ 0 $ 0 $ 0 $ 0 $ 0 $ 0 $ 0 $ 0

27 ============ ============ ============ ============ ============ ============ ============ ============

28 Full Gross‑up Full Gross‑up Full Gross‑up 1/2 yr full Partial g‑up Partial g‑up

29 TOTAL REFUND $ 0 1/2 yr partial

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